Funding and Administering Public Interest Energy Efficiency Programs

The Report of the Energy Efficiency Working Group

In Response to the
California Public Utilities Commission
Decision 94-12-063

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EXECUTIVE SUMMARY

The California Public Utilities Commission's (CPUC) interim decision proposes the development of a non-bypassable public goods charge (PGC) to fund public goods research and development (RD&D) and energy efficiency activities. This report provides recommended approaches (for energy efficiency only) to begin implementation of this decision by identifying what types of energy efficiency activities should be funded, options for the scope and magnitude of funding, and proposals for the administration of these funds. The principle recommendations in this report are summarized below.

TYPES OF ACTIVITIES TO BE FUNDED

The working group recommends that all current energy efficiency program activities administered by utilities should be initially eligible for PGC funding. However, the strategies used to promote efficiency investments and the design of these programs will need to shift to meet the CPUC's stated goal of market transformation. All Parties also agree that the new administrator should have the discretion to decide, within the adopted guidelines on a case by case basis, whether or not proposed program designs are consistent with the CPUC's market transformation objectives and its guidance not to pursue those activities that will normally be pursued by the private market. This case by case review is necessary because the use of a wide variety of program strategies, including customer incentives, is expected to offer the most effective approach to transforming markets. Indeed, any attempt to affect the structure of the market must address the needs of individual customers.

MARKET TRANSFORMATION GOALS

Most Parties support an interim definition[i] of market transformation and provide a series of potential program guidelines that the CPUC should consider. Parties disagree on the need for the CPUC to adopt specific definitions, policies, or design guidelines immediately as part of the mission statement for a new administrator. Some Parties recommend adoption of specific guidelines to ensure that the CPUC's goal of funding only those activities that will not be provided by the market is achieved. Other Parties recommend that the CPUC should not adopt any policy guidelines now until more is decided about the structure, capabilities, and resources of the new administrator. These Parties suggest the CPUC should delegate the task of deciding whether or not proposed program designs are consistent with its market transformation goals to the new administrator or defer this decision until later. The report also contains an analysis of the market barriers addressed by current energy efficiency program designs and recommended guidelines for use in ensuring that publicly funded activities are not displacing private market activities or sales.

[i] The interim definition proposed is "market transformation activities are designed to achieve long-lasting changes in the structure or operation of the market by reducing market barriers to the adoption of cost beneficial energy efficiency measures to the point where further public intervention is no longer appropriate in that specific market segment."

SCOPE

Most Parties in the Working Group support the development of a surcharge that collects funds from all natural gas and electricity users subject to the CPUC's jurisdiction. This is because of the need to ensure the surcharge is non-bypassable, does not encourage fuel switching, and is fair to all market participants. They also support continued use of public funds to encourage energy efficiency investments in both the electricity and natural gas markets and oppose a sole focus on electricity, particularly since most customers receive both gas and electricity from utilities. Southern California Gas (SCG) disagrees with these views. SCG strongly recommends that gas users should not be subject to the PGC because: (1) the gas industry has already been restructured and gas energy efficiency programs are already efficiently administered by gas utilities; and (2) SCG might be competitively disadvantaged if electric municipal utilities do not collect a PGC while investor-owned utilities (IOU) collect a PGC within SCG's service territory.

INITIAL LEVEL OR MAGNITUDE OF FUNDING REQUIRED

Parties recommend initial annual funding levels that range from $197 million to $427 million per year. The low end of the range corresponds to the energy efficiency program expenditures authorized by the CPUC for investor-owned utilities in 1996. This is equivalent to 0.84 percent of revenues from the investor-owned gas and electric utilities (equal to 1.1 percent of electricity revenues only). The higher level, $427 million, corresponds to actual spending on electric and gas demand-side management (DSM) programs (energy efficiency plus load management, fuel substitution, load retention and direct assistance programs) by investor-owned utilities in 1994, the year restructuring began. This is equivalent to 1.8 percent of electric and natural gas revenues (equal to 2.4 percent of electric revenues). Other Parties recommend using either the 1994 level of expenditure on only energy efficiency programs, which was $331 million, or the annual average expenditures on DSM programs from 1988-1994, which was $367 million. One member recommends that the specific surcharge level should be negotiated with each investor-owned utility or municipal utility based on their financial circumstances. Finally, some Parties maintain that setting a surcharge funding level is premature until other decisions are made about the scope of market transformation programs and restructuring in general.

STRUCTURE AND COLLECTION

Most Parties agree that the CPUC should collect the PGC based on energy consumption or a charge per kilowatt hour. This could also be done as a percentage charge on the entire electricity or natural gas bill. Some members recommend deferring a decision on this issue because it needs to be resolved consistent with the rate designs being considered to collect the competitive transition charge.

ADMINISTRATIVE OPTIONS

Parties recommend a range of new administrative structures to set policy, administer PGC funds, and deliver energy efficiency programs or activities. Most proposals create new policy or administrative boards to implement the CPUC's general policy directions and new mechanisms to ensure independent administration of the funds and effective delivery of program services to all market participants. Key differences among the proposals include the role of utilities in administering these programs, (from a prominent role to no role), who controls the PGC funds,

whether administrative organizations can also have affiliates who compete for these funds (proposals range from no to a conditional yes), the mix and voting rights of public and private members of the governing boards, and who should perform market assessment and program evaluation functions. A detailed overview of the differences in the proposals is shown in matrix form on page 4-3.

JURISDICTIONAL ISSUES

Most Parties believe that the public goods surcharge would ideally be collected from all customers, including those of municipal utilities, to ensure a level playing field and that all of the beneficiaries of these public programs also pay for them. The CPUC, however, does not have jurisdiction to adopt a statewide PGC. Parties proposed four strategies to deal with this issue: (1) adopt a PGC for customers of investor-owned utilities and later seek legislation that would require municipal utilities to collect a PGC from retail customers; (2) immediately seek legislation to establish a statewide PGC; (3) seek legislative authority to have all distribution utilities collect the PGC now but allow municipal utilities to continue to control and administer these funds; and, (4) adopt the PGC now for customers of investor-owned utilities only.

ACTIONS FOR THE NEAR TERM

Chapter 5 provides a list of actions the CPUC should take within the next 18 months to build the foundation for the new administrative structure. Most Parties recommend that the CPUC encourage Parties to begin laying the foundation for the pursuit of market transformation objectives by pilot testing new concepts, program activities, and approaches to measure the market effects of these activities. The Parties also recommend that the CPUC initiate a proceeding in early 1997 to develop guidelines and reporting rules for the new administrator, as well as to consider any necessary changes to the CPUC's DSM policy rules. Finally, all Parties recommend that the CPUC consider the impact of some key decisions being made in other restructuring forums on the capabilities and the effectiveness of the administrative structure chosen as a result of this report.

Chapter 1

INTRODUCTION

This report is submitted by the Energy Efficiency Working Group in response to the California Public Utilities Commission's (CPUC) decisions and rulings in its restructuring proceeding. The CPUC has asked the Working Group to provide information regarding the types of energy efficiency activities to be funded through the Public Goods Charge (PGC), the magnitude of this charge, how it is to be collected, and administration of activities to be funded by the charge.

The Parties to the Working Group believe that public intervention to encourage cost-effective energy efficiency not naturally provided by the market is justified in view of the market barriers to efficiency investment that pervade our economy.[1] These market barriers, which cannot be overcome by individuals or firms acting independently, obstruct the adoption of what would otherwise be cost-beneficial energy efficiency actions. An important role exists for public intervention aimed at reducing, removing, or overcoming market barriers to avoid the loss of widespread economic and environmental benefits from increased efficiency and to ensure continued transformation of the market for energy efficient products and services.

This report focuses on energy efficiency issues related to the PGC. The Working Group has attempted to follow the general policies provided by the CPUC, while addressing additional issues and options as they have arisen. It has taken an inclusive approach, ensuring that all Parties' views on relevant issues are included for the CPUC's consideration.

The issues related to energy efficiency are complex and cover a wide spectrum. Parties who have participated in the Working Group represent a variety of companies, agencies, and interests that may be strongly affected by restructuring. The following quote from an ancient philosopher provides some perspective on the group's deliberations within the context of changing market institutions:

It must be remembered
that there is nothing more difficult to plan,
more doubtful of success,
nor more dangerous to manage,
than the creation of a new system.
For the initiator has the enmity
of all who would profit
by the preservation of the old institutions
and merely lukewarm defenders
in those who would gain by the new ones.
-N. Machiavelli

[1] Golove, W.H. and J.H. Eto, *Market Barriers to energy Efficiency: A Critical Reappraisal of the Rationale for Public Policies to Promote Energy Efficiency*, Lawrence Berkeley Laboratory Report No. LBL-38059, Berkeley, CA: Energy and Environment Division, Lawrence Berkeley National Laboratory, 1996.

It should be noted that some members felt that the term "lukewarm" was not an adequate description of the conduct of either the "defenders" or the "advocates" in this Working Group. Indeed, all parties approached these issues with a level of passion and commitment not normally observed in a working group process.

The Working Group attempted to reach consensus on issues wherever possible, and this report identifies the areas where this effort was successful. It also describes areas where consensus was not reached, with discussions of differences and Parties' positions regarding the issues. In some areas there is still more work required on details, and some of the administrative proposals call for implementation details to be determined by various entities. The Working Group believes that the information presented in this report, together with the individual comments to be provided by Group participants following the report's completion, provides the CPUC with adequate information to establish a structure for collecting and administering the funds to support energy efficiency activities that would not be carried out by the private market. The Working Group is prepared to continue in any efforts desired by the CPUC to enable this result.

ENERGY EFFICIENCY WORKING GROUP

This Working Group began meeting in February 1996 in anticipation of CPUC direction for stakeholders to evaluate energy efficiency issues. Meetings were held from February through August, in both San Francisco and Sacramento. The Working Group was open to all interested Parties and was comprised of many Parties interested in energy efficiency issues. A listing of Working Group participants is included in Appendix D. Michael Messenger of the California Energy Commission (CEC) Staff acted as the Working Group's facilitator, assisted by Gail Mancarti. Meetings were scheduled and agendas developed with input from the Parties, and all members were encouraged to participate in discussions in and outside of the meeting process. This report was written by volunteers from the Working Group, with the entire Group's input and assistance. A group of editors was given the task of finalizing and editing the report after the drafts had received extensive review and revision by the Working Group. Mike Messenger was responsible for including all of the final editorial changes and takes responsibility for any errors or omissions. The final draft was also reviewed by all members of the Working Group, with the goal of including all points of view as accurately as possible.

WORKING GROUP MISSION STATEMENT

The Working Group agreed early in the process on the following mission statement regarding its efforts in preparing this report.

> The Group's mission is to produce a timely and informative report that responds to the major issues related to energy efficiency programs/activities identified in the CPUC restructuring order and provides recommendations and sufficient background on related issues to ensure an informed decision can be made.

BACKGROUND

Since the early 1980s, California has encouraged energy efficiency efforts through its regulated utilities, with emphasis in various areas as needs have changed and arisen. California has long been viewed as a leader in the country due to its successes in achieving significant energy efficiency results through these activities.

The Legislature and CPUC have adopted and promoted policies to ensure that cost-effective energy efficiency has been effectively pursued so that California could reap the benefits of these achievements. CPUC Code Section 701.1 requirements are summarized in Chapter 2. The CPUC has developed an extensive list of rules related to utility demand-side management (DSM) activities, protocols for measurement and evaluation, and a shareholder incentive mechanism designed to encourage utilities to maximize net resource benefits. Since 1977, the combination of regulatory and non-regulatory efforts has saved California consumers at least $13 billion.[2]

The CPUC, in its restructuring decisions, has continued the state's commitment to the public policy objectives related to energy efficiency. It has recognized that many of its policies and procedures for pursuing these objectives through the state's regulated utilities must change in light of the changes which will occur in a restructured electric industry. The CPUC has supported a non-bypassable charge to fund energy efficiency and other public interest activities. It has asked the Working Group to investigate necessary changes related to this charge and the manner in which energy efficiency has been delivered in the past which may be desirable under restructuring. Key citations from the CPUC decisions are presented in Table 1-1 at the end of this chapter.

THE NEED FOR CONTINUED PUBLIC SUPPORT FOR INVESTMENT IN ENERGY EFFICIENCY

As the electricity supply system becomes more competitive, most Parties believe that public sector efforts to improve energy efficiency will become even more critical than they have been in the past. Great gains in economic efficiency are anticipated as generators and distributors of electric power compete for large customers. Concern has been growing, however, for some Parties, that lower prices, especially for larger customers free to negotiate exclusive supply contracts, may increase total energy consumption, and that structural changes, along with existing, unremediated market failures, may create higher bills for smaller users -- especially residential and small business customers. This will increase environmental and resource-depletion costs, encourage greater resource inefficiency, and increase inequity at the same time funding for energy efficiency activities designed to mitigate these impacts may be declining.

Most Parties agree that the major rationales for public participation in the markets have not changed: the costs to society of environmental damage, resource depletion, energy dependence, and volatile prices are still not fully included in the private cost of energy; information about those costs that could help consumers make more efficient choices is still difficult to obtain and

[2] California Energy Commission, *Draft Energy Efficiency Report*, June 1996.

hard to act on; and most choices of energy-using technologies currently provided by the market still reflect a long history of artificially low energy prices. The market does not now, and will not, especially in the absence of public sector intervention, reach a societally optimum level of investment for energy efficient products and services in the foreseeable future.

The shift in focus of energy efficiency efforts from an emphasis on resource value to an emphasis on market transformation will not eliminate or reduce the need for continued public support for these activities. To continue the essential task of realizing public benefits by increasing efficiency, the non-bypassable PGC indorsed by the CPUC is necessary to fund cost-effective, market transforming energy efficiency activities.

STRUCTURE OF REPORT

This report is structured as follows:

Chapter 2 discusses the CPUC's original goals for energy efficiency activities and how restructuring and the CPUC's interim decision will affect the strategies and approaches used to achieve these goals in the future. The CPUC's interim guidance with respect to program design is assessed and interim design guidelines are discussed. It concludes with a review of the market barriers addressed by current energy efficiency programs and recommendations on the types of activities that should be eligible for PGC funding.

Chapter 3 provides recommendations on the scope, magnitude, structure, and collection of the PGC endorsed in the CPUC's decision. These sections contain recommendations on which customers should pay the PGC, how much funding is necessary to support energy efficiency policy objectives, and how these funds should be collected.

Chapter 4 discusses the principal functions of the new organizations responsible for the administration and implementation of PGC funds. It includes summaries of Parties' proposals for a new administrative structure and a discussion of the key similarities and differences between the seven proposals. This chapter also presents criteria for the CPUC to consider in evaluating these proposals.

Chapter 5 addresses the key issues the CPUC needs to address over the next 18 months in order to bring the new administrative structure on line. Within this context the chapter also identifies a number of key decisions in related restructuring forums that are expected to have a significant affect on the capabilities and effectiveness of the new administrator. As such, the CPUC should strive to coordinate these decisions with the decisions they make after reviewing the options within this report.

This response has four appendices. Appendix A contain a complete description of each of the seven major administrative structures proposed. Appendix B is a foundation paper on market transformation. Appendix C is a list of the acronyms used throughout the report, and Appendix D lists the organizations that participated in the Working Group.

The following table contains the CPUC's statements in its restructuring decisions related to energy efficiency and indicates the chapters of this report in which these statements are addressed.

Table 1.1 Citations From CPUC Restructuring Decisions	Chapter
Energy Efficiency:	
"The focus of publicly-funded energy efficiency programs should shift to those programs that are in the broader public interest, for example, programs with market transformation effects and education efforts that would not otherwise be provided by the competitive market." (COL 82)	2
"As discussed in our policy decision, we require additional information to allow us to establish the types of energy efficiency activities to be funded through the surcharge. As we obtain this information, we may modify our definition of appropriately funded activities or change the level to be collected. In addition, we would like to explore how utility expertise can be utilized as we shift to independent administration of these funds." (Road map, 3.c, Energy Efficiency)	2
"Customer specific energy efficiency projects should not require future funding from ratepayers, but should instead rely on market-driven mechanisms." (COL 83)	2
"Customer funding is appropriate for activities that are designed to transform the energy efficiency market and will not naturally be provided by a competitive market." (COL 84)	2
"The primary motive behind utility investment in energy efficiency has been to defer or avoid the high costs of new generation. However in a restructured environment, evaluating cost-effectiveness on the basis of utility resource deferral may no longer be as relevant." (p. 154)	2 2
All of page 155.	
"We propose a non-bypassable surcharge, the public goods charge (PGC), on retail sales to fund public goods RD&D and energy efficiency activities." (p. 145)	3
"By Jan 1 1997, energy efficiency costs should no longer be embedded in electric rates and instead should be collected as part of the public goods charge applied to retail electric sales." (COL 85)	3
"We will, therefore, delay the January 1, 1997 changes to bills until all such line items and surcharges are determined, no later than January 1, 1998." (Roadmap, 3.c, Energy Efficiency)	3
"Initially the line item rate should be set for each utility's service territory to correspond to authorized DSM funding. We will modify the level to be collected once we determine the appropriate level of public funding consistent with the above discussion and the workshops we anticipate conducting as part of our implementation of this decision." (p. 157)	3
"Over time, we prefer to see the same surcharge applied consistently across all utilities' service territories." (p. 157)	3
"Gas utilities should also participate in this process to ensure consistent treatment of comparable costs among competitors." (Footnote 63, p. 157)	3
"Because Legislation to ensure the surcharge is non-bypassable is desirable, we will likely ask that the workshops be used to assist us developing proposed language for that legislation." (p. 158)	3
"After a short transition period, we believe the funds collected through a surcharge for energy efficiency should be competitively allocated by an independent, nonprofit organization, but we would like to capture the expertise and knowledge that the utilities have gained in administering DSM programs as we begin the transition. We expect to reach closure on this issue through the implementation activities we will undertake in the next few months and through ongoing coordination with the Legislature." (p. 156)	4
"If we order workshops, we will direct workshop participants to explore the details of an independent administrator of these funds and the transition period to move to an independent administrator. How utility expertise can be captured should be explored as well." (p. 157-158)	4

Chapter 2

ACTIVITIES ELIGIBLE FOR PUBLIC GOODS CHARGE FUNDS

This chapter responds to the CPUC's request for additional information and recommended activities that should be eligible for funding under the PGC. The chapter provides an interim definition of market transformation, potential program design guidelines, a discussion of the market barriers addressed by current energy efficiency programs and recommended activities and program strategies to pursue with PGC funds.

CHAPTER ORGANIZATION

The first section discusses the Legislature and the CPUC's original goals for utility energy efficiency programs and how restructuring and the CPUC's Decision will affect the strategies and approaches used to pursue these goals in the future. The following sections discusses the definitions of market transformation, and then the CPUC's guidance in its decision with respect to program design, including the role of customer-specific activities, and the program design guidelines recommended by some members of the Working Group. The types of energy efficiency programs that should be funded by the PGC to achieve market transformation effects and additional actions that should be taken to make these programs more effective is discussed next. The final sections provide additional policy recommendations from some Parties and then summarizes the principal recommendations from this chapter.

THE PUBLIC-POLICY OBJECTIVES OF ENERGY EFFICIENCY PROGRAMS

What Are the Current Public-Policy Goals of Energy Efficiency Programs?

Section 701.1 of the PUC Code establishes the legal basis for utility ratepayer-funded energy efficiency programs. The code defines the principal goals of utility resource planning as: (1) to minimize the cost to society of reliable energy services, (2) to improve the environment, and (3) to encourage diversity of energy sources through improvements in energy efficiency (among other things). It also directs utilities to exploit all practicable and cost-effective conservation or energy efficiency improvements that offer equivalent or better system reliability and that are not being exploited by any other entity.

The CPUC offered the following guidance on the appropriate public policy goals and objectives for energy efficiency programs.

> *State policy supports utility pursuit of energy efficiency which is not pursued by other entities (see PUC 701.1). We have promoted utility involvement in these programs to ensure Californians received the benefits of energy efficiency, consistent with our resource procurement goal of providing least-cost, reliable, environmentally sensitive energy services. The primary motive behind utility investment in energy efficiency has been to defer or avoid the high cost of new generation. However, in a restructured environment, evaluating cost-effectiveness on the basis of resource deferral may no longer be as relevant. (Decision 95-12-063, page 155)*

The focus of publicly funded energy efficiency programs should shift to those programs that are in the broader public interest, for example, programs with market transformation effects and education efforts that would not otherwise be provided by the competitive market. (Decision 95-12-063, Conclusion of Law 82)

The Parties believe that the process of restructuring the electricity market should not change the basic policy goal of promoting cost-beneficial energy efficiency investments as outlined in current legislation and CPUC policy. The Parties, however, believe that the historic strategies employed to achieve these goals must be re-evaluated and modified to reflect basic changes in the electricity industry. New program designs or delivery mechanisms may be needed to respond to changes in both market conditions and CPUC policy.

All Parties support an increased emphasis on achieving the CPUC's market transformation goals. They also support consideration of policies to increase customer value and pursue a higher quality environment as discussed below.

The Parties' believe that establishing conditions conducive to the *maximization of customer value* should take on increased importance in the design of PGC-funded energy efficiency activities. Customer value comes from all aspects of a good or service. The customer's perspective is already partially embodied in one of the CPUC's benefit-cost tests, the participant test. As the relevance of the other tests changes, the Parties believe that the achievement of customer value deserves increased emphasis. The Parties, however, also acknowledge that the pursuit of customer value alone, may not fully reflect societal preferences with regard to the environment. Therefore, the Parties recommend the CPUC reaffirm the importance of *environmental protection*as a rationale for PGC funding.

Finally, restructuring offers an opportunity to place new emphasis on other public policy goals that were supported by some, but not all, Group members. They suggest energy efficiency activities should be designed to: (1) increase the range of meaningful choices available to customers; (2) reduce energy bills and provide other customer benefits for the energy services received; (3) help reduce environmental impacts; and (4) help mitigate the market power of supply-side resource-providers by increasing the price elasticity of demand by providing customers with better access to energy efficiency options.

Most Parties believe that current energy efficiency programs can be redesigned to achieve most if not all of these policy objectives. The California Energy Commission (CEC) Staff believe it is premature to determine whether or not, and to what extent, current energy efficiency programs can be redesigned to effectively realize the aforementioned market transformation objectives. Below we discuss the definition of market transformation and how it could be used to provide additional guidance on effective program designs.

THE DEFINITION OF MARKET TRANSFORMATION

The concept of market transformation figures prominently in Decision 95-12-063, yet the CPUC acknowledges that there are differences of opinion on what it means. The CPUC's guidance on this topic includes the following citations:

> *Customer funding is appropriate for activities that are designed to transform the energy efficiency market and will not naturally be provided by a competitive market. (Decision 95-12-063, Conclusion of Law 84)* and
>
> *It may also be appropriate to continue to provide financial incentives for energy efficiency products and services. Any such financial incentives should be focused on transforming the market for energy efficient products and services; some examples of these activities are the Super-Efficient Refrigeration Program, and manufacturer rebates for compact fluorescent light bulbs and high-efficiency motors. We expect that public funding would be needed only for specified and limited periods of time, to cause the market to be transformed. Given our focus on market transformation efforts, we disagree with DRA's comments that surcharge funds should be predominantly be used as a source of capital for the installation of demand-reducing technologies and measures. (Decision 95-12-063, pages 156-157)*

The Working Group spent a considerable amount of time discussing how this guidance could be used to craft a working definition of market transformation. Members of the Working Group initially provided two definitions that focussed on two key aspects of market transformation, the need to create lasting changes in the market and the need to work towards a goal of reducing barriers in the market to the point where public intervention is no longer appropriate. Eventually, most of the Group agreed on a synthesis of the two definitions as shown below. Parties disagreed, however, on the importance of adopting this particular definition of market transformation for use by the new administrator.

> *Publicly funded market transformation activities are designed to achieve long-lasting changes in the structure or operation of the market by reducing market barriers to the adoption of cost beneficial energy efficiency measures to the point where further public intervention is no longer appropriate in that specific market segment.*

SESCO believes that "market transformation" should refer to PGC funded activities that will "accomplish the most cost effective actual energy conservation; taking fully into account the effects upon people or businesses not directly assisted (the "non-participants") by the activity and the effects of the activity on the future choices of participants."

This definition is based on several underlying observations. First, customers today may face a variety of market barriers inhibiting adoption of cost-beneficial energy-efficiency measures. Second, the goal of energy-efficiency policy is to lower or reduce or overcome these barriers. Third, there are many strategies for lowering market barriers; different market barriers, moreover, may require different strategies. Fourth, intervention in a specific market segment is no longer needed once market barriers have been lowered permanently or to the point where the intervention is no longer cost-effective.

This interim definition of market transformation is consciously intended to reinforce the Parties' view of the appropriate role of the private sector in delivering energy efficient equipment. All Parties believe a guiding principle of PGC funding should be to create the conditions where competitive delivery of energy efficiency products and services can thrive and PGC funding for these activities is no longer required. Thus, energy efficiency activities should be designed to transform the specific market targeted to the point where intervention is no longer appropriate. The Parties recognize that, at this time, it is impossible to identify a date by when any specific market will be transformed. In addition, there may be intractable market barriers in some markets that require continuous public intervention. In sum, all Parties believe it should be up to the administrator or governing board to determine if publicly funded market transformation efforts have been successful, i.e., if and when further public intervention is no longer appropriate or cost-effective on a case by case basis.

Members of the Group had different perspectives on the importance of adopting a definition now and how the definition might be translated into more practical program guidelines as discussed below.

Two positions emerged with respect to the potential use of this interim definition. Some Parties recommend that the CPUC should use this interim definition of market transformation to guide the initial use of PGC funds but reserve any formal action until more experience with the market transformation programs is developed. These Parties also maintain that any market transformation definition should be presented to the administrator later on in this process as part of a larger package of directions that detail how the entire administrative organization should operate**.**

Other Parties recommend that the CPUC consider including a specific definition of market transformation within its proposed mission statement for the new administrator. Absent this definition, these Parties fear the administrator will continue to approve current program designs without reviewing the approach proposed to see if it is consistent with the CPUC's guidance in this area.

Both sides of this debate agree that a definition and related policy guidelines will eventually need to be adopted but disagree on the timing of when a definition of market transformation is needed. All Parties also agree that it is important to set up a process that will allow the definition of market transformation and related design guidelines to change over time as more experience is acquired.

PROGRAM DESIGN GUIDELINES

CPUC Guidance

In its restructuring decision, the CPUC signaled a desire to see some changes in the design of energy efficiency programs. The CPUC offered the following guidance from this decision.

> *In general, it is appropriate to use public funds to ensure that energy users have information about managing their energy use. It may be appropriate to have more public resources available for educating residential and small business customers than large electricity users, because large users generally have more resources to dedicate to managing their energy use. (Decision 95-12-063, page 155) and*
>
> *It may also be appropriate to continue to provide financial incentives for energy efficiency products and services. Any such financial incentives should be focused on transforming the market for energy efficient products and services; some examples of these activities are the Super-Efficient Refrigeration Program, and manufacturer rebates for compact fluorescent light bulbs and high-efficiency motors. We expect that public funding would be needed only for specified and limited periods of time, to cause the market to be transformed* (page 156)

The CPUC also indicated what types of program designs it did not support as shown in the following citation:

> *Customer specific energy efficiency projects should not require future funding from ratepayers, but should instead rely on market-driven mechanisms* (Conclusion of Law 83)

This section addresses each of these three citations. First, we address the more general issue of what types of changes in program design will be necessary to achieve the new market transformation objectives.

Working Group members had different perspectives on the best way to encourage a shift in energy efficiency program designs or strategies to achieve the CPUC's market transformation objectives.

Most Parties agree that it will be necessary to develop policy guidelines that are adopted by the CPUC to guide the expenditure of PGC funds. These guidelines will be necessary to ensure that PGC funds are effectively and efficiently spent and directed at achieving the CPUC's market transformation objectives. However, these Parties recommend that the CPUC defer adoption of specific policy guidelines until after the CPUC has resolved the issues of PGC administration and funding. These Parties believe that adoption of guidelines now would be premature and is unnecessary. In particular, the adoption of guidelines that are not well supported, that have been well thought out, and that are not based on empirical evidence could result in a focus on unproductive activities and the elimination of activities that have not been shown to be beneficial. These Parties believe that deferring this task would allow for more careful consideration of the issues and for the development of guidelines that are appropriate to the particular implementation strategy that is adopted by the CPUC. **This approach is supported by 14 members of the Working Group who chose to endorse a specific approach here.**

Two Parties recommend that the CPUC should explicitly adopt policy guidelines to ensure PGC funds are **primarily** spent on programs that create long-lasting market transformations by explicitly targeting the reduction of market barriers not likely to be addressed in the private market. These Parties suggest that in order to assure a smooth transition, activities directed at reducing market barriers should be phased in while those traditional cash rebate/subsidy programs that do not address specific market barriers are phased out. This policy would allow administrators to continue to fund some more traditional financial assistance programs during the transition to a new approach based primarily on reducing market barriers. **This approach is supported by the CEC Staff and SCG.**

What Specific Guidelines Should Be Adopted by the Administrator to Guide Program Design?

Despite these differences on the need to develop specific "market transformation guidelines," the Parties do agree that there will be a need at some point for the CPUC to provide some guidance to the administrator on program design. The following is a list of illustrative examples of key design principles or program emphases that could be used to guide market transformation activities:

- Design emphasis on changing the structure of the market to encourage the adoption of cost beneficial energy efficiency technologies.

- A design geared toward affecting the market as a whole, rather than solely achieving immediate customer-specific energy savings.

- A design geared towards causing market changes that persist without continual public intervention beyond maintenance or monitoring of the changed structure.

- Design emphasis on promoting customer choice and feedback on the performance of energy-efficient products.

- Design emphasis on achieving substantial and verifiable energy, resource and pollution savings that persist over the long term.

- Design emphasis that fosters the growth of the energy efficiency market.

<u>CEC Staff Recommendations</u>

In addition to these general guidelines, the CEC Staff recommends that the CPUC adopt guidelines specifically aimed at assuring a smooth programmatic transition to new initiatives designed to meet its market transformation objectives. CPUC guidance in Conclusions of Law 82, 83, and 84 (D 95-12-063 page 214) provides a valuable impetus for more fully exploiting major advances over the last 20 years in our knowledge about how to reduce market barriers.[3]

[3] Appendix B contains an Energy Commission Staff prepared foundation paper which summarizes these advances.

Because these advances do not fit easily into the prevailing utility DSM paradigm, which places emphasis on financial incentives and technical information, they have not yet been widely applied. The impetus for change due to restructuring thus offers a unique opportunity to more fully exploit this accumulated knowledge. But because they are likely to involve dramatic shifts in program emphasis the new market barrier reducing initiatives which build on this knowledge must be pilot tested and fine tuned before they can be implemented. And because they compete with the traditional DSM paradigm the ability to nurture the necessary embryonic innovation is endangered by the normal desire to justify the continuation of existing program categories and reinforcing measurement protocols. To overcome the inevitable resistance to change and take advantage of a uniquely promising opportunity, the CPUC should establish guidelines that make provisions, within whatever new administrative structure it chooses, for testing and, once proven, championing the new market barrier reducing initiatives. These guidelines should include the following:

- Adequate staff and funds should be made available to explore, pilot test for practicality, and ultimately champion innovative approaches directed at sustainable reduction in market barriers.

- To prevent any gap or abrupt shock in energy efficiency markets new activities directed at reducing market barrier should be phased in while subsidies are phased out (with the exception clarified below) during a transition period.

- After the transition, financial incentives should only be used in combination with other market barrier reducing strategies and limited to products not yet established in competitive market rather than to subsidize proven products.

- The current emphasis on program load impact measurement should shift from concentration on quantitative estimates of energy savings to include qualitative indicators on the degree to which market barriers reducing initiatives realize lasting improvements in market structure and performance.

How Will the Design of Market Transformation Activities Funded by the PGC Differ from Business-As-Usual Energy Efficiency Programs Funded by Utility Ratepayers?
While some Parties recommend continuing to use the existing energy efficiency program categories as a means of identifying and classifying potential PGC-funded activities, they do not advocate a return to business-as-usual program designs to meet market transformation objectives. These Parties expect that the design emphasis of most energy efficiency programs will shift *significantly* from programs which rely on cash incentives to influence individual energy efficiency purchase decisions to programs that transform markets and lead to lasting beneficial changes for all customers in the markets in which these decisions take place. Thus, these Parties feel that the recommendation to rely on existing program categories for classifying energy efficiency activities should not be confused with a recommendation to continue reliance on traditional energy efficiency program designs.

Can Market Transformation Objectives Be Achieved Through Customer-Specific Financial Assistance Programs?

As previously noted, the CPUC offered two sets of guidance with respect to the use of PGC funding for financial assistance:

> Guidance 3. *Customer specific energy efficiency projects should not require future funding from ratepayers, but should instead rely on market-driven mechanisms.* (Conclusion of Law 83) and
>
> Guidance 2. *It may also be appropriate to continue to provide financial incentives for energy efficiency products and services. Any such financial incentives should be focused on transforming the market for energy efficient products and services; some examples of these activities are the Super-Efficient Refrigeration Program, and manufacturer rebates for compact fluorescent light bulbs and high-efficiency motors. We expect that public funding would be needed only for specified and limited periods of time, to cause the market to be transformed.*(Page 156)

The Working Group spent several meetings trying to interpret the meaning of these two directives. In the end, most Parties agree that the CPUC's fundamental intent is included in their phrase, "Any such financial incentives should be focused on transforming the market for energy efficient products and services." Each directive in the decision returns to this theme of transforming markets. This conclusion led to the emphasis on carefully defining market transformation in this report and then analyzing what types of PGC-funded activities, in addition to the program examples suggested in the Decision, could meet the CPUC's test of "transforming markets."

It is the nature of the market to depend ultimately upon individual customer decisions. To succeed, all “market-driven mechanisms” for transforming markets must establish a means for causing customers to improve their decisions. Hence, all market transformation efforts must have "customer-specific" effects. It is in this sense that the term “customer-specific” is used in the following discussion.

Program designs which provide customer-specific financial assistance for energy efficiency projects currently represent a significant fraction of total utility DSM spending. These activities have accounted for the lion’s share of energy and bill savings from utility DSM programs. As a result, these programs may have contributed significantly to the success of utility DSM programs in transforming markets. Programs that include customer-specific activities (including both energy management services and financial assistance) can be designed to transform markets in the broader public interest and should, therefore, continue to be an option for PGC funding.

There is a second reason not to rule out the use of cash rebates and other customer specific financial assistance. The ability of programs that do not offer customer-specific financial incentives to transform markets is often enhanced by the programs that do offer them. For example, one archetypal market transformation strategy involves working “upstream” of customers with manufacturers. A critical element in the success of these programs, which are aimed at lowering the market barriers of these upstream producers, is the simultaneous offering

of “downstream” programs, which may involve financial assistance aimed at directly or indirectly lowering market barriers faced by customers. Constraining these programs to a “one-legged” approach would seriously cripple their ability to transform markets.

In the final analysis, the extent to which PGC funds are spent for customer-specific assistance, should depend entirely on the extent to which these activities are found to be an effective and practical means for transforming markets and, for some Parties, reducing energy consumption. Hence, the Parties wish to stress that, while they support continued funding for customer-specific assistance defined in this manner (i.e., for the purpose of transforming markets), they do not support PGC funding for the purpose of subsidizing product sales per se or for the competitive objectives of benefitting specific customers in a discriminatory fashion, to the exclusion of others.

SESCO does not agree with the above paragraph, because it fails to identify " whose competitive objectives are forwarded by "benefitting specific customers" or what the language "discriminatory fashion to the exclusion of others" means.

This interpretation of the CPUC's guidance with respect to customer-specific assistance will be used for the remainder of the report in order to move to the question of what specific types of activities should be eligible for PGC funding. The Parties request that the CPUC clarify its guidance in its next decision if this interpretation needs some refinement.

How Can Current Programs Be Redesigned to Meet the CPUC's Stated Objectives of Providing More Information to Residential and Small Commercial Customers on How to Manage Their Energy Use?

> *In general, it is appropriate to use public funding to ensure that energy users have information about managing their energy use. It may be appropriate to have more public resources available for educating residential and small business customers than large electricity users, because large users generally have more resources to dedicate to managing their energy use.* (Decision 95-012-063, Page 153)

Programs designed to improve small customer energy efficiency awareness should be a major component of the PGC portfolio. Some Parties recommend that the portfolio of PGC programs include promoting innovative pilot projects, such as the development of new, more user friendly billing formats and or new metering and communication devices. Existing residential and commercial information programs could be utilized to explore this concept as well as experimenting with new forms of metering and communication technology that can provide customers with feedback on the performance of their energy efficient equipment.

Who Should Determine Whether Specific Programs, Either New or Current, Meet the Guidelines That Are Ultimately Adopted in this Area?

All Parties agree that the new administrator(s) should be granted the flexibility to recommend or determine **if** the use of customer specific assistance is appropriate for any given market segment after carefully reviewing both the market barriers targeted by the program and any evidence that this strategy has been or is likely to be successful. The use of customer-specific assistance programs could be an important strategy to create a sustainable private energy efficiency services industry that should not be summarily removed by program design guidelines.

Designing new institutions or mechanisms to measure the success of these market transformation programs or activities should be a high priority for the new administrator. It is important to ensure that this new institution or research group is rewarded for pursuing independent market research.

WHAT TYPES OF ENERGY-EFFICIENCY ACTIVITIES SHOULD BE ELIGIBLE FOR PGC FUNDING?

The preceding sections have addressed alternative definitions of market transformation and the CPUC's suggested changes to energy efficiency program designs or strategies. The CPUC indicated that its guidance could change as more information was developed by the Working Group. This section provides this additional information on the program objectives of energy efficiency programs currently administered by utilities and their potential to transform markets.

This section begins by addressing the CPUC's direction that PGC funds should not be used to support activities that would be normally carried out by the private market. The Parties propose guidelines to support this objective and a preliminary list of activities that are not expected to be adequately provided by the private market. From these guidelines and the list we proceed to a review of existing program reporting categories for energy efficiency programs and a discussion of the key market barriers addressed by each program type. The section concludes with recommendations on what types of energy efficiency programs should be supported by PGC funds based on these market barriers and the program guidelines recommended in the first section.

Ensuring Public Funds Are Not Used to Provide Energy Efficient Goods or Services Normally Provided by the Private Market

The Parties reaffirm the Legislature’s basic goal for publicly funded programs: to pursue only those energy efficiency opportunities not pursued by others because of significant market barriers to energy efficiency faced by customers. PGC funding is not appropriate for activities that duplicate those services or products already provided by the competitive market. PGC activities should be designed to increase the scope and amount of private sector energy efficiency offerings and empower customers to evaluate these new options.

Most Parties agree that most of the current energy efficiency programs have the potential to transform markets. What is essential is not the type of program, but the potential of the specific program design to reduce market barriers not likely to be addressed by the private market.

There are at least three reasons why a cost effective energy efficiency activity or service might not be provided by private energy service providers:

- Providing the goods or services is not profitable because the benefits produced are public goods and the cost of the service cannot be recovered in private markets.

- Providing the good or service is risky if there are no effective market or feedback mechanisms that can be used by customers to differentiate quality service providers.

- Pervasive market barriers that inhibit customer access to capital or create high search costs for new products act as a severe constraint to private firm entry into this market.

The new administrator should consider these principles when attempting to identify what activities would not normally be provided by private firms.

Different types of programs and program designs can be used to address these market barriers that are not adequately addressed by private firms.[4] Below we provide a more complete listing of the activities or services provided by the different categories of current (or energy efficiency) programs. Following each category is an assessment of how these programs or activities can be used to address key market barriers and then a recommendation on whether or not these programs should be eligible for PGC funds.

Current Energy Efficiency Activities Funded by Utility Ratepayers

The DSM Policy Rules provide a detailed listing of the energy efficiency activities currently supported by utility ratepayers. These activities primarily deal with addressing market barriers to the adoption of commercially available technologies as opposed to performing basic or applied research on new or emerging technologies. The potential need to use PGC funds to address research and development needs for emerging energy efficiency technologies is covered in a different Working Group report.

There are four basic categories of energy efficiency programs: *(1) Customer-specific energy management services*; (2) *Customer-specific financial assistance*; (3) *Market-specific activities directed at classes of market participants*; (4) *Planning and evaluation activities*.

Customer-specific energy management services: These include activities currently reported as Residential Energy Management Services (EMS), Commercial EMS, Industrial EMS, and Agricultural EMS.[5] These services generally involve providing technical assistance and reliable information (e.g., audits) to customers on the expected energy impacts of installing a variety of

[4] For example, the provision of credible information on energy efficiency or product use through efficiency ratings or product labels is a public good that is not usually provided by private firms and helps consumers to differentiate between different levels of quality without incurring extensive search costs.

[5] Full descriptions of these program types can be found in the CPUC's DSM Policy Rules.

equipment options to help them make better energy-efficiency related decisions. Key market barriers addressed include:

- High search costs; by reducing the customer's time and effort needed to identify and price high efficiency equipment.

- Product performance uncertainties; by providing customized analyses of the expected energy impact of installing specific technologies.

- The unbalanced flow of information between suppliers and customers: by providing listings of available contractors and an independent analysis of the costs and benefits of spending additional dollars for more efficient equipment or process changes.

All Parties recommend that all of the programs in this category should be eligible for PGC funding because they meet the CPUC's objective of transforming the market by addressing the market barriers identified above and achieving cost beneficial savings for these customers. (SESCO last minute)

Customer-specific financial assistance: These include activities currently reported as Residential Weatherization Retrofit Incentives, Appliance Efficiency Incentives, Commercial Energy Efficiency Incentives (EEI), Industrial EEI, and Agricultural EEI. Assistance generally involves financial payments or financing arrangements that reduce the first cost or cost of capital of energy-efficiency measures. Reducing the first cost of energy efficiency products by providing financial assistance is a common strategy used by these programs to overcome a variety of market barriers. This category would also include the use of a standard performance contracting process that offers fixed prices/kWh saved to contractors and customers who can deliver verified energy savings. Key market barriers addressed by providing financial assistance include:

- Access to financing -- programs can provide loans or innovative payment options.

- Owner or builder decision processes bound by custom -- cash incentives can help restructure or revise decision making processes by making owners more aware of energy efficiency investment opportunities.

- Misplaced or split incentives between owners and tenants -- decision making process is improved by subsidizing planning and specification assistance for owners who may be indifferent to the energy bills paid by tenants.

- Product or service unavailability -- cash incentives can stimulate manufacturers to re-tool or stimulate distributors to stock more efficient models.

- High transaction costs -- cash rebates can make customers more aware of the existence and location of energy efficient products.

All Parties recommend that financial assistance programs should be eligible for PGC funding in so far as they clearly target the goal of reducing marker barriers. SESCO believes that these programs should also be required to produce cost effective savings, taking into account demonstrable market transformation effects.

*Market specific activities directed at specific classes of market participant*These non-customer specific activities are currently reported as Residential Information Programs, Residential New Construction, Other Residential Conservation Programs, Nonresidential Information Programs, Nonresidential New Construction, and Other Nonresidential Conservation/Energy Efficiency Programs. These activities generally provide information and financial assistance to different classes of energy service providers, such as architects or distributors, rather than to individual customers. The programs either address market barriers upstream of the customer (e.g., those faced by new home builders or more generally product suppliers) or aim to increase general customer awareness of energy efficiency.

Key market barriers addressed include reduction of product performance uncertainties through the use of demonstrations and monitoring of equipment performance, expansion or creation of new distribution channels that were restricted by custom or misplaced or split incentives between the occupants of buildings who may pay the bills and the building designers, contractors, and owners that pay for building construction.

All Parties recommend that all of the programs in this area should be eligible for PGC funding because they target specific market barriers, encourage the development of emerging technologies and have the potential to produce significant market transformation benefits for all customers by working with key energy service and efficiency providers. SESCO recommends that in addition to meeting these requirements, these programs should also have to demonstrate that they produce cost effective energy savings.

Planning and evaluation activities: These include activities currently reported under the Demand-Side Measurement, Forecasting, and Regulatory Reporting categories: Program Measurement, Demand-Side Forecasting and Planning, Load Metering, Saturation Surveys, Market Assessment and Other Research and Analysis, New Technology Assessment, Long-Range Planning and Forecasting, Regulatory Compliance and Reporting, Regulatory Reporting and Support, and Regulatory Oversight. These activities include the strategic planning and assessment functions used to support the design and improvements in most utility energy efficiency programs. They involve the collection of necessary market data to identify, target, and evaluate the effectiveness of programs designed to overcome specific market barriers to energy efficiency.

All Parties recommend that planning and evaluation activities be adequately funded to evaluate energy efficiency programs/activities because the results from these activities are essential to determine when public intervention is no longer necessary in a specific market segment and to develop recommendations to increase the effectiveness and reduce the cost of all PGC programs.

Summary -- The new administrator or governing board should strive to maintain a portfolio of program approaches and strategies from each of the four main categories listed above as well as consider funding for new and innovative programs designs that target the reduction of specific market barriers.

ADDITIONAL POLICY RECOMMENDATIONS

Some Parties provided additional recommendations related to specific actions or programs they felt the CPUC should consider and perhaps support in its final decision. They are not included with the body of other recommendations because the Working Group could not reach consensus on whether or not the CPUC had actually requested this type of specific recommendation.

CEC Staff Recommendations

CEC Staff recommend the CPUC encourage the following activities:

- Pilot testing and eventual large scale implementation of bill enhancements that would make it easier for customers to verify energy savings and bill reductions from their past actions and identify potential for future savings.

- Pilot testing and eventual implementation of independent quality inspection and rating services that make it easier for consumers to find energy efficiency service providers that they can have confidence in.

- Pilot testing and eventual implementation of low cost dispute resolution procedures that reduce consumer risks associated with the purchase of energy efficiency products.

Workshops to Discuss Market Barriers Not Likely to Be Addressed by Private Market

The CPUC should hold workshops in the near term to help forge a consensus on how to identify market barriers that are not likely to be addressed by the private market. To help refocus the designs of current energy efficiency programs will require a strategic focus on identifying and reducing market barriers to energy efficiency investment by testing new program designs. Progress will be accelerated if both regulators and the new program implementers can agree on a common set of market barriers to be addressed. The scoping study conducted by CADMAC contains a potential list of market barriers that could be used to start the discussion.

Encourage the Development of New Measurement Paradigms

The CPUC should encourage utilities or third parties to begin now to measure the effectiveness of current programs in transforming markets. The success of new PGC programs in furthering the CPUC's desire to transform markets objective rests on the extent to which the program is successful in reducing targeted market barriers. Some program activities have no doubt been more successful than others in transforming markets. Success, in this regard, is not a manner of certain program designs being ones that are inherently capable of transforming market, while others are inherently not. Instead, success depends on determining to what extent each program design has, in fact, lowered market barriers. This will require the development of a whole new discipline of measurement of market effects and quality control management.

Environmental Marketing Group Recommendations

The Environmental Marketing Group (EMG) recommends the CPUC support necessary rule changes and legislation to encourage programs with low or no direct PGC program costs. Examples cited for consideration include:

- Support consistent enforcement of energy efficient building and appliance standards.
- Promote use of energy efficiency mortgages.
- Mandate that the utility distribution companies (UDCs) provide customers with the ability to secure a loan that can be linked to their billing accounts for the purpose of financing energy efficiency measures.
- Coordinate and match funding for trade, engineering and design occupation energy efficiency skill training programs identified with energy efficiency program goals; especially where labor market shortages exist.
- Require billing information disclosure by customers in order to be eligible for program benefits.
- Require mandatory disclosure of utility account histories upon sale or transfer of property.
- Require/institute dual-account requirements on leased properties.

SUMMARY OF CONSENSUS RECOMMENDATIONS

1. PGC-funded activities should embrace a broad array of energy efficiency activities consistent with the objective of transforming markets to the point where intervention is no longer appropriate.
2. All current energy efficiency program activities, including customer-specific assistance, should be eligible for funding to the extent that they can demonstrate positive contributions to the objective of market transformation. At the same time, the Parties recognize and fully support the notion that re-focussing attention on this objective will require new program designs and should therefore not be confused with a call for a return to business as usual.
3. Planning and evaluation activities should be continued, but realigned to more closely support the market transformation objectives of PGC-funded activities. To accomplish this realignment, the CPUC should consider making changes to its current M&E protocols or delegating the important task of developing a new measurement system to the new administrator.

4. Two implementation options were identified by the Group: adopt either market transformation definitions or guidelines to govern program design now; or wait until after the Commission has resolved the issues of PGC administration and funding. The CPUC should carefully consider whether it is appropriate to provide more guidance on the mission of the new administrator through adoption of funding or policy guidelines or agree to defer this decision until later.

5. All Parties recommend that the new administrator (s) should be given the flexibility to determine or recommend whether the use of customer specific assistance is appropriate on a case by case basis for any given market segment.

Given these perspectives on what types of energy efficiency programs should be funded, the next chapter (3) addresses the important topic of how much money is needed to initially fund these programs and how to collect and disburse these funds. In Chapter 3, this question is put into historical perspective by reviewing energy efficiency program funding levels over the last decade and alternative methods to collect the PGC.

Chapter 3

THE NON-BYPASSABLE PUBLIC GOODS CHARGE: SCOPE, MAGNITUDE AND COLLECTION

INTRODUCTION

This chapter provides recommendations on the scope, magnitude, structure and collection of a PGC to support the energy efficiency goals and objectives described in Chapter 2. It contains the options, opinions and approaches recommended by Parties in the Working Group to actually implement the CPUC's decision. In areas where the Group has achieved a consensus on a particular policy or option, one recommendation is presented. In areas where Parties could not reach agreement, alternative recommendations or options are identified along with the Parties that support them. In areas where a consensus of the Group was reached and only one or two members held alternative views, the phrases "a majority of the Group" or "most Parties" is used. In areas where the Group's opinion was split, the phrases some Parties or other Parties is used.

Rationale for a Public Goods Charge

Members of the Group had different reasons for supporting the PGC for energy efficiency activities. Four major reasons emerged:

1. Adoption of the charge would remove the costs of these programs that are currently lumped into general energy rates and provide customers with valuable information on the actual costs of public policy programs;

2. Adoption of the charge would preserve the capability for society to promote investments in energy efficiency services and products;

3. Adoption of the charge would, if properly structured, help ensure that all energy consumers, regardless of where they obtain their power, pay for the energy efficiency programs that currently provide them with benefits; and

4. Adoption of the charge for electricity and natural gas users would remove an incentive for customers to try to avoid paying these costs by switching fuels or suppliers, thus receiving the benefits from these programs without paying for them.

Scope of Public Goods Charge (or who should pay?)

This section provides two types of recommendations: some that affect customers and utilities within CPUC jurisdiction (and can be implemented immediately) and others that may affect customers in non-jurisdictional utilities. Inclusion of non-jurisdictional customers will require either the passage of new legislation to implement or voluntary adoption by non-jurisdictional wholesale gas customers and/or municipal utilities.

There is a delicate tradeoff between the advantages of creating a PGC now for customers within the CPUC's jurisdiction and the possible disadvantage that taking action now for only these customers will lead to a fragmented and "unfair" market. Taking action now may lead to the collection of a PGC for customers of jurisdictional utilities while there would be no such charge collected for customers of non-jurisdictional utilities. This section presents issues related to the collection of these charges for customers within the CPUC's jurisdiction (Questions 1, 2, and 3) and then presents other issues related to the collection of PGC for customers completely or partially outside of the CPUC's jurisdiction (Questions 4, 5, and 6).

Question 1: Should All CPUC Jurisdictional Customers Be Required to Pay the PGC?
All Parties agree on the necessity of developing a surcharge mechanism if public policy programs are to continue in the restructured electricity market.[6] Most Parties also agree this surcharge should be levied on both retail electricity and gas customers connected to the distribution grids. However, since the gas industry has already been restructured and gas DSM programs for core customers are continuing to be administered by gas only investor-owned utilities, the need for a surcharge on gas customers is not supported by SCG.

In part, differences over the scope of customers who should pay the PGC reflect different perceptions of what types of customers are likely to benefit from programs funded by the PGC. Some Parties believe that both electricity and natural gas customers currently benefit from DSM programs and that the switch to the PGC is simply a change in the collection method for gas DSM programs rather than a "new policy." Other Parties perceive that the scope of the CPUC's order and proceedings is limited to the electricity industry. In addition, SCG believes a PGC is not needed to support the continued operation of gas utility DSM programs .

The majority of the Group was able to agree that as a minimum condition:

The public goods charge should be assessed at the meter to all jurisdictional retail customers connected to the electricity and natural gas grids.

Beyond this level of agreement, there was no clear consensus on how to treat specific customers who might attempt to bypass the PGC. The principal reasons for and against including certain types of customers within the PGC are presented below along with a discussion of what changes in legislation would be needed for the CPUC to ensure the PGC could be collected from each type of customer.

Question 2: Should the PGC Apply to Customers Who Generate All or a Portion of Their Electricity Needs? If So Should a Fee Be Charged for Both Their Natural Gas Use and the Electricity They Either Consume on Site or Resell to the Distribution Utility?
The Group recommends that the CPUC structure the charge so that energy customers are not required to pay the PGC twice, once as a surcharge on the gas purchased to fuel self or co-

[6] TURN and EMG's support for the surcharge is conditional on the rate being non bypassable for existing electricity customers.

generation units and again as a charge when customers purchase electricity at the retail level. Parties have different views on how to interpret or implement this principle. These are described below.

- Most Parties (ARCA, CEC, DRA, EMG, ICA, Onsite Energy, PG&E, SCE, NRDC, Proven Alternatives, Sierra Club, TURN) recommend that the exemption from the PGC should be limited to that portion of the total gas used by the customer to generate electricity while any remaining retail gas use should be subject to the PGC. These Parties suggest this policy would ensure that the PGC would only be levied on "retail" uses of gas such as the production of heat or the use of gas as a feedstock and not on wholesale uses of gas to produce electricity whose sale is subject to a separate PGC.

- Other Parties (SCG, DGS) assert that all customers who generate electricity on site (utility electric generators and self generators) should be exempt from paying the PGC on gas usage. These Parties recommend that self generation customers should be exempt from the PGC because they (particularly non-core gas customers) are not currently required to pay for any share of DSM programs. These Parties also maintain it is not worth the effort to secure new legislative authority to collect the PGC from non-jurisdictional customers at the state or even the federal level.

- The remaining Parties (SDG&E and CES/Way) feel resolution of this issue is primarily contingent on the method the CPUC ultimately adopts to collect stranded costs through the competition transition charge (CTC) for wholesale and/or self or co-generation customers. These Parties suggest that the CPUC should not try to resolve the self generation or cogeneration PGC issue until after a decision on how to collect the CTC from these customers is adopted.

  Most Parties believe that new legislation would be required to accomplish any of the three options proposed above if the CPUC proposes that non-jurisdictional gas customers be required to pay the PGC in order to discourage bypass of this charge.

Question 3: Should Some Jurisdictional Customers Be Allowed an Exemption from the PGC Because of Their Choice of a "Renewable" Electricity Supplier or If Their Home/ Building Passes a Threshold "High" Energy Efficiency Rating Established by the CPUC?
One party, the Environmental Marketing Group, recommends that some customers should be excluded from paying the PGC based on their voluntary choice to either purchase electricity generated from solar or renewable resources or purchase a more efficient building shell at home or at work. This party reasons that customers who upgrade their building/home to meet a high standard of energy efficient design or performance or who purchased electricity from a "renewables" supplier, should also be allowed to bypass the charge. The basic rationale for this exemption is that the individual customer/building site who qualifies for this exemption would have already mitigated the environmental impacts and/or achieved an energy efficiency standard that the surcharge was designed to address. This exemption would then drive private decisions on both supplier and consumer sides of the market towards achieving public policy goals. It would also be a major spur for ensuring accurate benefit cost ratio analysis by regulatory

authorities. Finally, EMG believes the type of customized billing procedure needed to exempt certain customers will be a fact of the restructured energy services marketplace.

All other Parties believe it is premature to begin granting exemptions from the PGC and reserve judgement on whether these types of objections should be allowed. They suggest the creation of any exemption from the PGC based on achievement of a high energy efficiency standard or renewables purchase requirement would be arbitrary and contestable in court. Even granting one PGC exemption now might encourage a significant number of petitions for exemptions by a variety of customers who felt they might be able to avoid the PGC if they demonstrated their "good intentions." Finally, these Parties are concerned that the costs of developing and maintaining a PGC exemption processing system would be significant.

Question 4: Should the PGC Also Apply to Customers Who Switch from Gas to Non-Regulated Fuels, Such as Propane?

SCG asserts that the PGC must also apply to those customers who have the ability to switch from natural gas to other non-regulated fuels such as propane **if** the PGC is collected from any gas customers. PG&E recommends that the PGC should be charged to any customers who switch from regulated to non-regulated fuels after the PGC begins to be collected. They reason that the PGC should not apply for all current users of propane because most of these customers are not currently required to pay for gas DSM programs. Both Parties reason that including these customers is important in order to ensure the PGC is truly non-bypassable for all customers who might benefit from the energy efficiency programs. This is particularly true for gas customers who currently have the option to choose between alternative pipeline suppliers or opt for using propane as an alternative to natural gas. To be completely non bypassable, the charge would have to be levied against all of these energy users, regardless of supplier or fuel type. One party (TURN) recommends taking the principle of including all fuel users one step further by developing a PGC collection mechanism for non-jurisdictional gas customers who purchase gas directly from interstate pipelines and are subject to FERC rather than CPUC jurisdiction. Any attempt to collect the PGC from customers who use non-regulated fuels would require legislation at the state and possibly the federal level.

The remaining Working Group members do not recommend setting up mechanisms to collect the PGC from customers who currently use non-regulated fuels (e.g., non-jurisdictional gas customers) for at least two reasons. First, these Parties assert that a charge ranging from 1 percent to 3 percent of customer bills or revenues is not large enough to actually cause most customers to switch fuels to avoid PGC payment. Second, the CPUC would need to seek legislative authority to collect these charges for non-jurisdictional customers or non-regulated fuels. These Parties reason that the costs and effort needed now to enforce such legislation does not justify the potential benefits of collecting the PGC from these customers.

Question 5: Should the CPUC Support Legislation to Ensure That the PGC Is Levied on All Electricity Distribution Customers in California, Including Those Customers Currently Served by Municipal Utilities?

Ideally, the PGC should apply to all customers receiving electric service to prevent the possibility of some customers choosing to bypass the charge by seeking service from utilities

who don't collect the PGC. However, the CPUC lacks the jurisdiction to require that all California customers pay this charge because roughly 25 percent of the state's residents are customers of municipal electric utilities. In large part, resolution of this dilemma may be a matter of choosing the right time to pursue a change within the more general structure of reciprocity agreements being negotiated between the investor-owned utilities and municipal utilities. The Working Group identified four options the CPUC should consider to deal with this problem:

- Adopt a PGC for customers of investor-owned utilities only for now and seek legislation that would require municipal utilities to establish a surcharge for their customers.

  This option would allow the CPUC to develop the new PGC collection and administration system for the investor-owned utilities now and postpone any potential conflict with municipal utilities over the issue of local control. It would also give the Legislature time to evaluate the severity of the bypass threat represented by having a PGC for CPUC-jurisdictional distribution companies and not others. Likewise, it would also allow all Parties time to evaluate the performance of the programs authorized by the new administrator. If the bypass threat proves to be real and many customers actually bypass the PGC, the CPUC could seek emergency legislation to ensure all customers must contribute to the charge. **Parties supporting this option include: ARCA, DRA, DGS, EMG, ICA, NRDC, Sierra Club, and SCG**

- Seek legislative authority to have the PGC apply to all electricity customers by Jan. 1, 1998 or as soon as possible, and make clear that the CPUC would then assume jurisdiction over the use of these funds. This would require an extensive outreach effort to educate and hopefully convince municipal boards of how the PGC would work and why relinquishing control over how this money is spent would benefit them or their customers. This option could be implemented by Jan. 1, 1998 if legislation is passed by July 1, 1997 and signed by the governor in 1997. **Parties supporting this option include: SCE**

- Seek legislative authority to require that all distribution utilities collect the PGC but allow municipal utilities to continue to administer and control the use of these funds.

  To ensure the funds are well spent, municipal boards might be periodically required to certify that the funds were being devoted to the public policy areas covered in the CPUC Decision or as listed in the new statute. SDG&E believes that legislation should also provide a method for ensuring that municipal utilities administer the funds consistent with the intent and objectives of the statewide procedures adopted for the investor-owned utilities. This option would give municipal utilities the option of collecting additional funds beyond the uniform PGC level if desired or voluntarily sending their PGC funds to the new administrator body approved by the CPUC. **Parties supporting this option include: CEC, CES/Way, EMG, TURN, Proven Alternatives, SDG&E, NRDC, & PG&E**

- Consider adoption of the PGC for customers of investor-owned utilities only because the CPUC Policy Decision did not explicitly indicate that this charge should apply to utilities not regulated by them.

  The City of Palo Alto supports this option because it is concerned about the potential loss of local control over the funds they currently use to run energy efficiency programs. Palo Alto argues it is imperative that City Councils and Municipal Governing Boards retain the ability to implement energy efficiency policies within their own jurisdictions because local authorities are more familiar with the needs and resources of their own utilities. **Parties supporting this option include: City of Palo Alto**

Question 6: How Can Customers of Non-Jurisdictional Distribution Utilities (Municipal or Out of State) Be Encouraged to Collect a PGC and Coordinate Their Efforts with the PGC Administration in California?

Some Parties recommend consideration of at least three options to encourage other utilities to join the PGC-funded system: entice non-jurisdictional utility participation by highlighting the benefits of new PGC programs to their customers; offering regulatory or reciprocity incentives to non- jurisdictional utilities; or conditioning the participation of other non-jurisdictional utilities interested in joining the California wholesale power exchange system with an agreement to collect the PGC.

MAGNITUDE OF THE PUBLIC GOODS CHARGE

Factors to Consider in Setting the Annual Funding Level For the PGC

The level of expenditures required to support energy efficiency programs through a PGC is a function of the goals adopted for the programs by the Legislature or government bodies, trends in energy prices, how well the private market for energy efficiency is functioning, the strategies proposed for the use of the funds, and the type of administration used to oversee how the funds are spent. Accordingly the amount of money necessary to achieve these goals is likely to change over time and should be modified periodically. This section first focuses on establishing the **initial** budget level. The next section discusses how these budgets might be modified over time.

The CPUC must decide whether to set the level of the PGC by its own order or through legislation. In its decision the CPUC gave the following guidance with respect to this topic:

> *Initially the line item rate (for the PGC) should be set for each utility's service territory to correspond to authorized DSM funding. We will modify the level to be collected once we determine the appropriate level of public funding consistent with the above discussion...(P. 157)*

This quote has been interpreted by some Parties as a directive to set the initial PGC level for 1998 programs at the authorized (1996) DSM funding levels. Another interpretation is that this was a directive to initially use the level of 1996 utility DSM budgets for 1997 programs and display it as a line item in customer bills beginning in 1997. These Parties argue this was not a recommendation to set the PGC for all activities that begin on Jan 1, 1998 at 1996 authorized levels. Parties with the second viewpoint suggest the CPUC has repeatedly stated it is interested

in hearing all analyses of what the "appropriate" level of public funding should be before they make a final funding level decision. Both interpretations are discussed in the next section. The following is a list of factors the Working Group members recommend that the CPUC should consider when determining the initial funding level:

- Historical funding requirements and current authorized budgets for DSM and energy efficiency programs operated by investor-owned utilities.

- The potential need for the new administrator to develop new forms of energy assistance/programs during an uncertain restructuring period.

- Changes in long-term funding requirements from programmatic and/or administrative shifts.

- The societal cost-effectiveness of previous utility programs and the potential need to mitigate market power or other problems identified in the environmental impact report produced for the restructuring proceeding.

Historical Data for Use in Developing an Initial PGC Funding Level

The next section provides information on historical funding levels for both DSM programs and energy efficiency programs. Table 3-1 provides a historical perspective on the amount of money expended on DSM,[7] energy efficiency and RD&D programs over the last seven years. It also displays the relationship between DSM, energy efficiency and RD&D expenditures as a percentage of electricity revenues from investor-owned utilities.[8] The table shows that DSM expenditures as a fraction of revenues have varied from 0.99 percent in 1988 to 2.21 percent in 1994, while expenditures on energy efficiency programs only ranged from 0.55 percent to 1.28 percent of 1994 revenues. These totals do not include shareholder incentive payments paid for program years 1991 through 1994. In 1994 incentive payments to utilities were $38 million, to be verified and then paid out over a period of 10 years. In 1995, utilities have requested earnings in excess of $100 million. This total award will be verified, adjusted if necessary, and then paid out over a period of 10 years.

The principal funding level recommendations from the Working Group were primarily derived by reference to these historical expenditure levels and currently authorized (1996) levels for DSM programs. Most members of the Group chose to first recommend an absolute dollar budget on the statewide level and then convert this to an equivalent percentage of electricity or electricity and natural gas revenues to ensure the charge is uniform. Other members chose to either recommend a percentage amount from the beginning for each utility distribution company or allow the amount of the PGC collected to be negotiated with each distribution utility. We first discuss the rationales for the recommended dollar amounts and then conclude with a

[7] Energy Efficiency programs are a subset of DSM programs. Expenditures on DSM programs include energy efficiency programs **and** funds spent on load management, fuel substitution, load retention and direct assistance programs.

[8] No data is available on the amount of public funds used to support the renewable industry in the last seven years but we understand this data may be produced in the Renewables Working Group report.

discussion of how these amounts could be converted to a percentage of total electricity or gas revenues at the service area level.

Table 3-1

Electric Utility DSM and RD&D Expenditures Versus Total Electric Revenue
From 1988 through 1995
in Nominal $ Millions

Statewide	1988	1989	1990	1991	1992	1993	1994	1995
RD&D Programs	102.4	110.9	98.0	121.3	106.5	103.9	114.6	66.9
DSM All Programs	126.1	152.4	189.0	323.3	339.6	351.6	385.5	278.9
DSM-EE-IOU Only	69.8	90.3	133.9	215.2	224.2	225.6	257.3	216.8
Electricity Revenues	12,745	14,604	15,376	16,025	16,913	16,779	17,411	16,901
DSM-EE/Revenues	0.55%	0.62%	0.87%	1.34%	1.33%	1.34%	1.48%	1.28%
DSM All/Revenues	0.99%	1.04%	1.23%	2.02%	2.01%	2.10%	2.21%	1.53%
DSM+RD&D/Revenues	1.79%	1.80%	1.87%	2.77%	2.64%	2.71%	2.87%	2.00%
RD&D/Revenues	0.80%	0.76%	0.64%	0.76%	0.63%	0.62%	0.66%	0.40%

Sources and Key

Revenue source: FERC FORM 1 ELECTRIC OPERATING REVENUES (ACCOUNT 400) LINE 27 for investor-owned utilities.

DSM Expenditure Source: Investor-Owned Utility Annual DSM Reports: 1981 through 1995.

DSM EE = IOU expenditures on energy efficiency programs.

DSM ALL = Utility energy efficiency, load management, fuel substitution and Measurement and Forecasting Expenditures.

RD&D expenditures take from draft Appendix on R&D expenditures for the RD&D Working Group, these totals exclude transportation research.

Statewide Funding Levels Recommended by the Parties

Table 3-2 includes the recommended PGC funding levels supported by the Parties and their relationship to historical program funding levels at the statewide level. These include the use of authorized or actual funding levels for energy efficiency or DSM programs in 1994, the use of currently authorized funding levels for energy efficiency or DSM programs in 1996, or the use of the average funding level for DSM programs from 1988 to the present. This is followed by a discussion of the rationale for each proposed funding level and the Parties that support them, as well as a discussion of the rationales for Parties that do not recommend a specific funding level.

Rationales or Reasons to Support Alternative Initial Funding Levels

Parties had different points of view on which historical funding data should be used to determine the initial funding level for the PGC. The major options supported by Working Group members and the reasons behind them are discussed below:

o Rationale for use of the $427 million actually spent by investor-owned utilities on DSM programs in 1994. **Parties supporting this level include: CES/Way**

Parties supporting this funding level believe the use of the actual expenditures on DSM programs of $427 million in 1994 is appropriate for two reasons. First, this was the amount that utilities voluntarily expended in pursuit of cost beneficial DSM investments that reduced the system cost of providing electricity before the uncertainties introduced by the April 1994 CPUC Decision that signaled its commitment to restructuring the electricity market.

Table 3-2

Recommended Statewide Annual Funding Levels

Scope and Year of Funding Options	Annual Spending Electric and Natural Gas-Investor-Owned Utilities (Millions)	Annual Spending Investor-Owned Electric Utilities Only (Millions)
1994 - All DSM Programs** -Actual	$427	$335
1994 - Energy Efficiency*- Actual	$331	$269
1996 - All DSM Programs- Authorized	$336	$240
1996 - Energy Efficiency*-Authorized	$197	$160
1988-1994 DSM Programs-Actual Average	$367	$267

* Energy Efficiency includes all energy efficiency cash incentive programs, all energy management service programs, new construction programs, information programs, measurement and evaluation and "other" programs. It does not include direct assistance or load management programs.These estimates were provided by utilities based on their Annual DSM reports filed with the CPUC in May of 1996.

** DSM programs includes all of the energy efficiency programs from above plus load management, fuel substitution, load retention and direct assistance programs

*** These figures do not include the shareholder incentive payments paid out for utility programs in 1994. For perspective, the authorized earnings for all four investor-owned utilities for their 1994 DSM programs totaled $38.4 million.

Second, they maintain that this program expenditure level produced the highest level of net resource savings ever achieved for California in a cost effective manner.

o Rationale for use of the $331 million actually spend on energy efficiency program by investor-owned utilities in 1994. **Parties supporting this level include: Proven Alternatives, and ARCA**

Parties supporting this option believe that the actual expenditures of $331 million for energy efficiency programs in 1994 is appropriate. First, this was the amount that utilities voluntarily expended in pursuit of cost beneficial energy efficiency investments before the

uncertainties introduced by the April 1994 CPUC Decision that signaled their commitment to restructuring the electricity market. The dollar amount is lower than the DSM total above because it excludes utility expenditures on direct assistance, load management and fuel substitution activities. They assert that the use of ratepayer funds for load management or fuel switching programs is no longer appropriate in a competitive generation market and thus should be subtracted from the DSM total. They also argue that the expenditures for low income or direct assistance programs should be subtracted out of the PGC charge because the CPUC Decision supports the use of a separate charge for direct assistance programs.

- Rationale for use the $197 million level currently authorized for energy efficiency programs run by investor-owned utilities. **Parties supporting this funding level include: DRA, ICA, PG&E, the Sierra Club and SCE**.

  Parties in support of this option believe that the CPUC ordered that the current or 1996 authorized DSM funding level be used on an interim basis to set the PGC surcharge level (as discussed earlier, see page 8 of this chapter).

  The 1996 authorized level is $336 million for all electric and gas DSM programs operated by investor-owned utilities (1.4 percent of 1994 revenues) and $197 million for energy efficiency programs only (0.8 percent of 1994 revenues). This lower level for energy efficiency programs excludes direct assistance programs, load management and fuel substitution programs.

  PG&E supports this option in principle because it is the closest to its position that its 1996 authorized funding levels for DSM and energy efficiency activities are the correct amounts to determine the initial level of PGC funding for activities supported by PG&E customers. However, they are concerned that converting this statewide amount on a uniform basis to the service area level might result in lower funding for PG&E than is currently authorized. As a result PG&E recommends that its current DSM (excluding load management and direct assistance programs) expenditure level of $105 million ($92 million electric and $13 million gas) be explicitly authorized for collection by the PGC for its service territory.

- Rationale for the use of the average DSM funding level from 1988 to 1994. **Parties supporting this funding level include: CEC Staff and NRDC**

  DSM program expenditures by investor-owned utilities averaged $367 million per year between 1988 and 1994 for electric and gas utilities. The annual expenditures on these programs averaged roughly **1.6** percent of annual gas and electric revenues during this same period. Proponents of this option believe that this long-term average level of program expenditures is likely to be more representative of funding requirements for energy efficiency programs because it takes into account the effect of changes in customer participation levels during periods of rising and falling energy prices. On the other hand, this average funding level may be contaminated by the adoption of shareholder incentives for DSM performance in 1991. Until then, investor-owned utilities had no strong motivation to propose aggressive funding levels to pursue DSM programs. Thus, this

average funding level may be too low if some form of performance incentives for the administrative organization are to be continued in the future or too high if performance incentives are to be phased out.

- Rationale for use of 1994 statewide expenditures on DSM programs funded by investor-owned and municipal electric utilities. **Parties supporting this funding level include: SCG**

  SCG recommends that the PGC must be collected statewide from all electric distribution utilities to ensure a level playing field between generation suppliers and utilities. This requires summing the expenditures of both investor-owned and municipal utilities to derive a total funding recommendation. Municipal electric utilities spent roughly $100 million on their DSM programs in 1994 as compared to $335 million spent by electric investor-owned utilities. The sum of all 1994 electric utility DSM program expenditures is $427 million or roughly 2.4 percent of all 1994 electric investor-owned utilities revenues. Adoption of this recommendation would require legislation to be enacted since municipal utilities are not subject to CPUC regulation.

- Insufficient data or premature to determine an initial funding level. **Parties supporting this funding level include: TURN, EMG, and SDG&E**

  Some Parties were not willing to choose a specific absolute dollar amount for energy efficiency programs from the tables above for the reasons discussed below. For example, TURN and EMG feel it is premature to identify a funding level for energy efficiency programs until a more detailed description of the programs or activities to be run or implemented is developed. They believe there is a need for a bottoms up budget analysis of funding requirements for energy efficiency programs for two reasons. First, future market conditions after restructuring are not likely to resemble the market for energy efficiency in the recent past. Second, the historical level of expenditures on energy efficiency programs is not necessarily relevant to the requirements of a new organization devoted to transforming energy efficiency markets or reducing new forms of market barriers in the post restructuring world. TURN recommends an analysis of what **new** energy efficiency service activities or programs should be funded and what these activities might cost to administer and implement. This might also include an analysis of which existing DSM program budgets could be reduced or are no longer needed as well as the potential need for new programs.

  SCG, TURN, EMG, and the CEC Staff support beginning this type of "bottoms up" analysis as soon as possible. The Working Group did not have the time or the resources to complete this type of bottoms up analysis. Most Parties recommend that the CPUC require that the new administrator or some independent body develop a bottoms up analysis of what funding level would be needed after the CPUC has chosen an organizational framework and issued whatever policy guidance is necessary. This analysis could provide the basis for a decision on PGC funding levels for use in the years immediately after the startup of the new administrator, perhaps in 1999 or 2000.

SDG&E did not provide a recommended funding level for energy efficiency programs for a different set of reasons. They believe that it is premature to establish dollar amounts for funding energy efficiency programs without considering the cumulative amount of funding that is proposed to support all public purpose programs. While it will be important to designate the amount of surcharges to be devoted to each public policy activity (energy efficiency, RD&D low income, etc.), this should be done as part of a coordinated effort that looks at all the surcharges together.

Conversion of Annual Statewide Funding Requirements to Specific Public Goods Charges at the Service Area Level

In theory, a uniform PGC could be collected at the state level and then allocated or distributed by an administrator to different geographic regions or service areas. In practice, most Parties support the collection of the PGC at the local distribution company level using a uniform percentage of revenues approach. Under this approach, the annual funding requirements would be collected using a uniform percentage of the total revenues collected by each utility. Whether this money is then more effectively spent by local or state level administrative bodies is the subject of Chapter 4. There are at least two different ways of establishing an overall budget for the PGC: adopting a fixed budget amount in current dollars or translating the budget into a fixed percentage of electricity revenues. Both are discussed below.

- Setting the PGC level as a fixed dollar amount at the state or service territory level. **Parties supporting the use of a fixed dollar budget to set the initial PGC include: SDG&E, TURN, PG&E, and SCG.**

  Each of these Parties oppose the development of an ongoing fixed surcharge or percentage of revenues approach for different reasons. First, TURN believes there is insufficient data or analysis available on the amount of money that would be needed to support energy efficiency programs that provide services not already provided by the private market. Second, SCG believes that the PGC budget should be set once at an absolute dollar level for each service territory (using historical data or other factors) and then be periodically changed via negotiation or by the administrator responsible for overseeing the effective use of these funds. SDG&E believes that a percentage of revenues approach should be used to set the initial dollar budget.

  TURN also argues that a percentage of revenue approach may be unfair to different customer classes that already pay high rates now and will have no chance to decrease their payment burden under a uniform collection approach. Finally, it believes the use of a percentage surcharge approach could stimulate PGC bypass strategies by retail marketers who will try to minimize the energy portion of the bills they charge to customers and collect their primary business costs through other contracting methods such as shared savings agreements.

  SDG&E recommends that the amount of the PGC should be set on a percentage of electricity revenues on a statewide basis to be consistent for all customers. However, the percentage should only be used to derive an initial PGC amount and that this percentage

should not be applied to revenue levels that will change in the future. This is because they believe it does not make sense to try to capture generation revenues in the future. The PGC amount could be changed after recommendations from the administrator, but any changes should be made on a uniform basis to that the percentage of revenues collected from each utility in California remained consistent. In addition SDG&E believes the funds collected by a UDC should be allocated to that UDC's service territory and customers.

PG&E supports a fixed dollar amount initially because the current differences in utility funding as a percentage of total revenues could cause funding at a given utility to significantly increase or decrease if a fixed percentage is applied to all customers. PG&E does support the adoption of a fixed percentage in the long run.

- Setting the PGC as a fixed percentage (or surcharge) of total electricity or natural gas revenues. **Parties supporting this approach include: DRA, CES Way, CEC, EMG, SCE, ARCA, Proven Alternatives, NRDC, Sierra Club, and ICA.**

  These Parties suggest the use of a percentage of revenues approach is more useful because it can be applied on a uniform basis and not discriminate between customers in different geographic regions. It would be useful for both the governing boards and the organizations in charge of delivering energy efficiency services because the revenues used to fund PGC programs would automatically adjust as a function of growth or declines in utility revenues. This approach would also allow the administrator(s) of funds to increase or decrease the PGC percentage level on a uniform and statewide basis based on market conditions. This approach would be superior to adopting a either a fixed statewide budget and attempting to allocate it to service territories or negotiating different budget levels for different service areas and running the risk of collecting disproportionate shares of customer bills in different geographic areas.

  Assuming that the CPUC adopts the surcharge approach proposed in its decision, it is important that the charge be specified as a percentage of **total** electricity or natural gas revenues (including generation, transmission and distribution services) rather than simply a percentage of the revenues collected by the distribution company. This is because the amount of the total customer electricity bill collected by the utility distribution company may change significantly as integrated utilities begin to unbundle their services.

  In sum, the use of a uniform percentage collection approach has the advantage that PGC budgets would automatically adjust upward and downward with annual revenues from the sales of electricity and natural gas. It has the disadvantage that it may be more and more difficult to track or estimate total revenues for the distribution, transmission and generation portion of integrated natural gas or electricity companies, particularly if distribution companies are functionally separated or completely divested from their generation affiliates.

  Table 3-3 shows the potential revenues that could be collected by a PGC set equivalent to 1 percent, 2 percent, and 3 percent of revenues for investor-owned electricity and natural gas utilities combined and for electricity utilities only. Recall that the range of annual funding

levels recommended by the Parties ranged from $197 million to $427 million. This suggests that the lower budget figure could be collected using a surcharge rate of 0.8 percent of all electric and natural gas revenues while the higher funding requirement could be collected by collecting a surcharge of just over 1.8 percent.

Integration of Energy Efficiency Funding Recommendations with the Funding Requirements for Other Public Goods Programs

The CPUC decision calls for the development of a surcharge to fund both energy efficiency and RD&D activities. The Working Group believes that the funding requirements set forth for energy efficiency activities above can simply be added to those levels the CPUC finds are necessary to pursue the other public policy goals to determine the aggregate PGC level. This is because there is little if any functional overlap between the energy efficiency market activities outlined here and the research and development activities considered in the RD&D Working Group.

Table 3-3

Potential PGC Funding Levels as a Percentage of 1994
Electric and Gas Revenues for Investor-Owned Utilities in California

1994 Annual Revenues (Millions)	1% of Annual Revenue (Millions)	2% of Annual Revenue (Millions)	3% of Annual Revenue (Millions)
Electric IOUs = $17,411	$174	$348	$522
All Electric Utilities = $21,013	$210	$420	$630
Electric and Gas IOUs = $22,340	$223	$446	$670
All Electric and Gas Utilities = $26,100	$260	$520	$780

The Memorandum of Understanding reached by SCE, IEP, CLECA and CMA suggested that a charge equivalent to 3.3 percent of revenues would be sufficient to meet these public policy needs. More recently a floor of 3 percent of all electricity revenues to fund public policy programs has been proposed in legislation (AB 1123) by Sher. A PGC equivalent to up to 3 percent of all electricity and natural gas revenues would be sufficient to meet the different funding levels suggested by members of the Energy Efficiency Working Group and our understanding of the levels proposed in the RD&D Working Group. Table 3-4 provides the surcharge rates that would be required to raise each Parties' recommended initial funding requirement for energy efficiency programs.

Table 3-4

Conversion of Initial Funding Levels to Surcharge Percentages
Based on 1994 Revenues for
Investor-Owned Electric and Gas Utilities

Annual Funding Level	Surcharge Required; % of Electric and Natural Gas Revenues; % of Electricity Revenue Only	Parties in Support of this Funding Level
$427 (1994 Actual DSM)	1.8%; 2.4% of Electricity Only	CES/Way
$367 (Average DSM)	1.6%; 2.03% of Electricity Only	CEC Staff and NRDC
$331 (1994 Actual EE)	1.4%; 1.83% of Electricity Only	EMG, Proven Alternatives, ARCA
$197 (1996 Author. EE)	0.84%; 1.1% of Electricity Only	DRA, Sierra Club, ICA, PG&E, and SCE
Negotiated		SCG
No Recommendation Now		TURN, EMG, SDG&E

A surcharge level of 3 percent of all electricity revenues could be used to cover all of the expenses of all public policy objectives identified in the CPUC order, including research and development, energy efficiency and any funds necessary to support emerging renewables technology. This rate would collect $540 million for investor-owned electric utilities, and roughly $630 million if applied to the $21 billion in 1994 revenues collected by all utilities, including municipals. The 3 percent surcharge would raise $705 million if applied to both gas and electric revenues for investor-owned utilities in 1994 and roughly $750 million if applied to all electricity and natural gas sales across the state.

Should the CPUC Recommend That Legislation Be Adopted to Establish Either a Floor or Ceiling Surcharge Rate for All Investor-Owned and/or Municipal Utilities?
The answers to this question are closely tied to Parties' positions about the need to strongly encourage and or mandate the participation of municipal utilities in the PGC. Three different options are recommended by Group members:

- Some Parties support the adoption of a common statewide percentage floor for PGC expenditures to be coupled with some minimum policy guidance in the legislation regarding what the money should be used for. **Supporters include: ARCA, DRA, EMG, ICA, CES Way, CEC Staff, SCE, NRDC, and the Sierra Club.** These Parties believe that developing a surcharge floor is necessary to demonstrate a consistent commitment to promote energy efficiency investment and allow for medium and long-term planning based on the assumption that these funds will be available.

- Some Parties support the adoption of a cap on PGC expenditures as a fraction of electricity and natural gas revenues. **Supporters include: EMG, PG&E, ICA, DGS and TURN.** Surcharge caps are necessary to ensure that the PGC administrator not be allowed to increase this budget beyond the specified level without the approval of the Legislature.

- **SCG** recommends that a PGC funding requirement be negotiated with each distribution utility based on their financial circumstances.

- **SDG&E** suggests it is not appropriate to identify PGC funding in terms of floors or caps. Once the Legislature or CPUC identifies a level of PGC funds to be spent on energy efficiency, there should be a requirement that the administrator attempt to spend all of the funds allocated. The administrator should also recommend whether or not the funding level should increase or decrease based on the results of the programs and the need for future funding in relationship to the goals set by the CPUC.

MODIFICATIONS TO PGC FUNDING LEVELS OVER TIME

After the initial surcharge level is set, provision should be made for modifications to this level to reflect the success or failure of these programs. How often these adjustments need to be made is in part a function of which administration and supporting delivery system options are chosen. Some Parties recommend that the initial funding level adopted by the CPUC be held constant until 2003 and that modifications be made by the appropriate body in the new administrative system. Other Parties recommend more frequent adjustments to the PGC funding level and an annual or biannual review of budgets by the CPUC, Legislature, or governing board. The specific processes recommended for modifications to funding levels under the different administrative options are outlined in Chapter 4.

STRUCTURE OF THE PUBLIC GOODS SURCHARGE

Relevant CPUC Guidance

The CPUC Decision states:

> *We suggest to the Legislature the adoption of a surcharge to fund energy efficiency activities as discussed above. The surcharge would be applied in the same manner as the CTC and be non bypassable. (p. 154)*

"Scope of PGC," on page 1 of this chapter, discusses the challenges related to ensuring the PGC is not easily bypassed by different types of customers. This section provides the rate design options to ensure PGC collection is compatible with the CTC rate design and is fair and equitable to all customer classes.

When Should the CPUC Adopt a Rate Design for Collecting the PGC?

Most Parties believe the CPUC should address rate design issues associated with the PGC after it deals with how to collect the CTC. However, the CPUC should first decide on an initial funding requirement for the PGC. Once this is determined, the details of the collection mechanism can then be resolved consistent with the mechanism that has been adopted for the collection of the CTC. Other Parties believe there is no logical relationship between the PGC and the CTC. They

assert that attempts to link the two charges and related issues could undermine public program efforts since the CTC may be the subject of complex and strenuous legal challenges.

What Method or Rate Design Should Be Used to Collect the Funds?
Some Parties agree that the PGC should be collected by the existing distribution utilities using the same rate design or method chosen to collect the CTC, if at all possible. Other Parties believe it is inappropriate to decide that the method chosen for the CTC will be appropriate for the PGC. This is because the method chosen for the CTC is likely to be a political compromise that may not be appropriate for the much smaller PGC.

Regardless of when the decision should be made, the principal rate design options are:

A. Collect the fees based on energy use (mills per kilowatt hour (kWh) or therm).
B. Collect the fees based on a demand charge ($ per peak or average kilowatt (kW) per month).
C. Collect the fees based on a surcharge (percentage) of the dollar amount of the monthly bill.
D. Defer a decision on any of these alternatives.

Discussion of Option A. An energy consumption based fee is supported for equity reasons (customers should pay a proportionate share based on their total energy use) and environmental reasons related to the need to discourage inefficient energy use. Some supporters of this option were strongly against the use of a percentage fee on the total bills because it was perceived to be inequitable to small customers. **Supporters of this option include: ARCA, EMG, TURN, NRDC, Proven Alternatives, and the Sierra Club**.

Discussion of Option B. No members of this Working Group supported Option B, the use of demand charges or fees to collect the PGC.

Discussion of Option C. One member, **the DRA**, supported the use of a surcharge (percentage) of the total customer bill to collect these fees for the situation where the UDC continues to bill end use customers. This position is reasonably consistent with Option A, which recommends that the fee be energy consumption based. Collecting the surcharge on the entire bill would necessarily include a fee on some of the demand or peak demand components, but these demand costs would be relatively small for most customers and zero for residential customers under current rate designs.

Discussion of Option D. Finally, the remaining Group members (**ICA, CEC, CES/Way, PG&E, SCE, SCG, & SDG&E**) recommend that the CPUC defer a decision on the preferred rate design at this time. They recommend using a rate design option that is consistent with the method ultimately chosen to collect CTC revenue requirements to ensure consistent rate treatment and simplicity. These members have not developed a preferred position on what rate design option is best for collecting the PGC.

How Should the Introduction of the PGC Rate Design Be Coordinated with Unbundling of Other Items on the Customer Bill and Subsequent Display to Customers?

The CPUC Decision states:

> *Assuming the Legislature adopts a PGC, it should initially be a line item on utility bills and then change to a surcharge, depending on when legislation adopting the surcharge is enacted.*

This suggests that the PGC would first appear on the bill as a dollar line item and that its introduction needs to be carefully coordinated with the appearance of other line items for unbundling of electricity services called for in the CPUC Decision. This policy makes sense because it would minimize the transition costs to a new billing format and thus customer confusion. It is recommended that whatever changes in billing format the CPUC approves for the PGC should coincide with the first unbundling of distribution, transmission and generation functions and costs now set for mid-1998. Most Parties had no strong preference with respect to the issue of how the PGC should appear on bills and whether separate amounts for expenditures on different public policy objectives need to be displayed.

Others feel that what costs are disclosed on the bill is a crucial issue. For example, NRDC suggested that there must be full disclosure of costs of producing and delivering electricity from different types of generation rather than requiring partial disclosure of the costs of public policy programs through a line item with no corresponding line items for other important costs. SDG&E believes there should be one line item on the bill that includes the costs of all public purpose charges, such as energy efficiency, RD&D and low income programs, to avoid the confusion that would be caused by listing a multitude of line items on the bill.

Should Funds Be Separately Collected for Energy Efficiency and RD&D Programs?

Most members recommend that the PGC be set at a level to fund both energy efficiency programs and research and development programs. Other Parties feel strongly that RD&D programs should be funded separately. (SCG at a minimum.) SDG&E and EMG believe that the PGC should cover both energy efficiency and RD&D programs, but that the specific amounts allocated to each area should be determined in advance, at the time the PGC level is established. This principle should be followed independent of which administrative option is adopted.

The method of allocating these dollars after collection varies depending on the administrative options and public goods delivery schemes outlined in Chapter 4. Under some options, the funds are spent by the same body which collects the PGC and in other proposals the funds are expended by different entities. The actual mechanism used to disburse and keep track of PGC funds should be developed after the decision on administrative structure is made.

HOW MUCH WOULD THE PGC COST THE AVERAGE CONSUMER?

It is important to remember that a PGC is not a new tax but simply a different way of funding expenditures on energy efficiency programs. The Group decided it would be useful to provide the Legislature with some background information on current levels of DSM program expenditures and how they relate to typical customer bills.

The following calculations provide some perspective on the current costs of funding utility programs on a per energy unit and per customer basis. An across the board charge of 2 mills per kWh or roughly 2 percent of 1994 electric utility revenues would have provided sufficient funding ($360 million) to cover spending for all electric utility energy efficiency programs in 1994.[9] This charge would cost the average residential electricity customer a little over $1 per month or roughly $14 per year.[10] This is roughly 2 percent of the average residential electricity bill of $650 per year. (Using a typical consumption level of 7,000 kWh per household.) Similar calculations find that funding the 1994 natural gas DSM program level of $92 million would cost the average residential natural gas consumer 6 mills per therm or roughly $4 per year for an average consumption level of 600 therms per year. This cost is roughly 1.2 percent of the total average gas bill of $380 per year.

Table 3-5 shows the typical cost to customers at different PGC funding levels ranging from $200 million to $360 million.

Table 3-5

Cost of PGC to Typical Residential Customers
for Different Statewide Budget Levels

PGC Statewide Level (Millions)	Annual Cost to Average Residential Electric Customer (IOU)	Annual Cost to Residential Natural Gas Customer(IOU)
$200	$7	$2
$360	$14	$4

[9] In 1994, California utilities spent $335 million on electric DSM programs and $92 million on gas DSM utilities. This works out to an average cost of 1.8 mills per kWh to fund electric programs and 6 mills per therm to fund natural gas programs.

[10] This estimate does not include the potential revenue losses to the utility created by energy efficiency programs.

Chapter 4

OPTIONS FOR THE ADMINISTRATION OF THE PUBLIC GOODS CHARGE

This Chapter responds to the CPUC's request for additional information about and recommendations for the administration of funds collected for energy efficiency through a PGC mechanism. The first section cites the relevant passages and conclusions of law from Decision 95-12-063. The Parties have proposed seven separate administrative options to achieve the CPUC's goals of an independent administrator for PGC funds. The next section describes the categories used to compare these proposals based on the functions that need to be performed to successfully implement and evaluate energy efficiency programs designed to transform specific markets. This section also provides information on the structure of the seven different proposals. This data is presented in a matrix format that highlights which organizations or market participants will be responsible for completing the key functions in each proposal. The following sections provide an analysis of the differences and similarities between the proposals, and list criteria the Parties recommend the CPUC consider in reviewing the proposals. The final section provides two page summaries of each party's proposal for an administrative structure. A more complete description of each administrative proposal can be found in the Appendix A of this report.

ISSUES FROM DECISION 95-12-063 ADDRESSED IN THIS CHAPTER

The discussion and proposals in this chapter are intended to respond to the CPUC's desire to establish an independent administrator for PGC funds. The CPUC's guidance to the Working Group on the administration of PGC funds is cited below:

> *After a short transition period, we believe funds collected through a surcharge for energy efficiency should be competitively allocated by an independent, nonprofit organization, but we would like to capture the expertise and knowledge that utilities have gained in administering DSM programs as we begin the transition.*(page 157)

A FRAMEWORK FOR COMPARING PROPOSALS FOR ADMINISTRATION OF PGC FUNDS

Parties have sponsored eight distinct proposals or proposed structures for administration of PGC funds. The differences (and similarities) between these proposals are best seen in the ways each option identifies the responsible Parties for: (1) policy setting; (2) administration and management; (3) market and program assessment; and (4) program implementation. The description of the proposals summarized in the following section are organized using these categories. The next section provides more details on the tasks included in each of these four categories. Table 4-1 lists who is responsible for these functions and tasks (see next page).

Policy Setting includes identification of who will be responsible for setting policy regarding what activities will be funded by the PGC and ensuring these funds are spent effectively to match state policy objectives. This includes a discussion of who will be responsible for selecting the members of the governing board, who will be accountable for the oversight of organizations charged with administration and management of PGC funds, and who will be responsible for setting overall

Table 4-1

Identification of Who Performs what Functions in Each Proposed EE Administration and Delivery System

Function	Subcategory What gets done	(1) CEEX DRA, TURN and SESCO	(2) EEFC Sierra Club	(3) Energy Efficiency Board*	(4) Current System SoCal Gas	(5) CEEPIRB CEC Staff	(6) Independ. Admin. DGS	(7) Elected Boards (EMG)
Policy Setting	**Select/Define Members of Governing Board/ Establish PGC Scope & Broad Policy**	CPUC or Legislature	CPUC or Joint Powers Agreement if Statewide	CPUC	CPUC is Governing Board	CPUC or Joint Powers Authority	CPUC/CEC Staff	CPUC in stage 1; ratepayers and directors in stage 2
	Oversight of Administration of PGC funds	Governing Board	CPUC or JPA if Statewide	Statewide Energy Efficiency Board (EE Board)	UDC, DSM Advisory Com with CPUC Approval	Governing Board	Governing Board	State and Local Boards
	Establish Program Guidelines & or Budgets	Governing Board	Energy Efficiency Fund Corp.	EE Board	CPUC and UDC	Governing Board	Governing Board	CPERB- State Board
	Adjudicate Policy Disputes & enforce Board decisions	Governing Board	EEFC with Limit Appeals to CPUC	EE Board with limited appeals to CPUC	CPUC	Governing Board	Governing Board	CPUC&Regula-tory Oversight Office (ROO)
Admini-stration and Manage-ment	**Develop Specific Programs/Activity Budgets**	Independent Administration of Energy Efficiency (IAEE)	Market Participants & EEFC Consultants	UDCs with oversight EE Board	UDC with DSM Advisory Committee Input	Statewide or Local Administrators (LA's)	Governing Board	CPERB for General; Local Boards for Specific Activities
	Procure Services (Develop RFPs and or Std Performance Contracts)	IAEE *DGS or competitive bidding in the SESCO	EEFC Contractors & UDCs	UDCs with EE Board oversight	UDC & 3rd Party Providers	Local Admini-strator (UDCs, non profit, or local govt.)	DGS - Office of Energy Assessments	Independent Administrator
	Track and Report on PGC Spending	IAEE *DGS or competitive bidding in the SESCO Variant	EEFC Staff	UDCs with EE Board oversight	UDC & 3rd Parties	Statewide or Local Administrators	DGS - Office of Fiscal Services	Independent Administrator

Table 4-1
(Continued)

Identification of Who Performs what Functions in Each Proposed EE Administration and Delivery System

Function	Subcategory What gets done	(1) CEEX- DRA, TURN & SESCO	(2) EEFC Sierra Club	(3) Energy Efficiency Board*	(4) Current System SoCal Gas	(5) CEEPIRB CEC Staff	(6) Independ Administ. DGS	(7) Elected Boards (EMG)
Implementation of Market Transform-ation Activities	**Deliver Statewide or National Upstream Activities: Non-customer Specific**	IAEE Contracts with ESPs	EEFC & Contractors	UDCs with EE Board oversight	UDC with DSM Advisory Committee Input	Statewide Administrators under Board guidelines	As the Board Determines	CPERB- State Board
	Deliver Local or Regional Programs: Non-customer Specific	IAEE Contracts with ESPs	EEFC & Contractors	UDC and ESCOs with EE Board oversight	UDC with DSM Advisory. Committee Input	Local Administrators Under Board Guidelines	DGS	Facilitators and Local Boards
	Deliver Customer-Specific Energy Services and or Equipment	Energy Service Providers (ESPs)	Energy Service Providers (ESPs)	Energy Service Companies and Customers	UDC & Third Party Providers	Local Administrator Contracts with Qualified ESPs	Energy Service Providers through Voucher System	Qualified Service Providers Per CPERB Guidelines; Facilitators
Market Barrier Assessment and Program Evaluation	**Assess Progress in Meeting Market Objectives/Reducing Market Barriers**	Market Assessment Group	CPUC Advisory Committee	EE Board with UDC Input	UDC, DSM Advisory Comm with CPUC Approval	State Level Assessment Group (SAG)	Board, CEC Staff, DGS, Other Stakeholders	CPERB:ROO
	Recommend New Designs/ Pilot Tests Based on Research & Evaluation	Market Assessment Group	CPUC Advisory Committee	UDCs, EE Board Staff and other stakeholders	UDC, DSM Advisory Comm (DAC) and CPUC	Stragetic Assessment	Board	CPERB and Local Boards
	Verify Specific Program Energy Savings or Program Effectiveness	ESPs and Assessment Group	EEFC & Consultants	ESCOs, UDC and Customers	UDC & DAC with CPUC Approval	Stragetic Assessment	DGS	CPERB:ROO

* Members supporting the Statewide Energy Efficiency Board include CES/Way, EDF, Enova Energy, NRDC, NAESCO, PG&E, Proven Alternatives, Onsite Energy, SCE, SDG&E and Rocky Mountain Institute. These names are not listed on the top row due to space limitations. Hereafter this Group of Parties is referred to as the Coalition.

policy guidelines and or budget priorities. Finally, this function includes the responsibility to enforce and adjudicate policy disputes and review, and perhaps approve, proposals to modify the strategies used to achieve objectives.

Administration and Management describes the entities responsible for operational oversight of PGC funds. These responsibilities include program design; proposing budgets for specific programs and activities within the overall guidance provided above; procuring providers to deliver services or programs within approved budgets (including developing requests for proposals when needed); and tracking and reporting on PGC spending.

Implementation describes which entities or firms would be involved in the delivery of various types of PGC-funded energy efficiency services or activities. This category includes a description of (1) who would be eligible and responsible for implementing Board plans to effectively participate in regional/national upstream market transformation efforts; (2)who would be responsible for delivering more targeted, non-customer specific energy efficiency services or programs intended primarily to transform California or regional markets; and (3) who would deliver customer-specific energy services (such as the installation of more efficient equipment).

Market Barrier Assessment and Program Evaluation describes the entities or market participants responsible for planning and evaluation activities. These responsibilities include assessing overall progress by the programs in meeting specific market objectives and/or achieving reductions in market barriers; recommending new program designs and pilot programs based on these assessments and other evaluation research; and measuring the performance of specific programs either by verifying the energy savings achieved or gathering market data on other measures of program effectiveness.

The next section presents the key similarities and differences between the proposals.

KEY SIMILARITIES AND DIFFERENCES BETWEEN THE PROPOSALS

Common Features in Policy Setting

Setting Policies -- All Parties agree that the CPUC, or some CPUC recognized governing board, should set the basic policies that will guide collection, funds allocation, program design and implementation of PGC activities. Each proposal also establishes some form of new board, either administrative or governing. The particular functions performed by the board in each proposal are different. Some proposals include a new administrative board chosen by an existing governing body to implement programs while other proposals create new governing boards with significant policy setting functions including program design and establishing budgets.

Pursuit of Market Transformation -- All Parties agree that the new board or the policy setting body should adopt guidelines to ensure pursuit of market transformation objectives.

Conflict of Interest Rules -- All Parties agree that the financial interests of board members and the potential for self dealing must be addressed. Most Parties also agree that conflict of interest rules and disclosure requirements should be required of board members.

Key Differences in Policy Setting

Strength of Governing Board -- Parties disagree about the need for a new governing board, the types of authority the governing board can exercise over the administrator, the role of and how many staff would be needed to help set board policy, and, the degree to which board decisions can be over ridden by existing energy agencies or a new body formed through a joint powers agreement. Proposals range from the establishment of a very small staff to provide administrative support to the board members only (the Coalition) to the establishment of larger staff sufficient to develop pilot projects and champion program initiatives targeted at reducing market barriers. (CEC Staff)

Representation of Public and Private Interests on the Board -- Parties disagree about how to ensure that both private and public interests are represented on the governing boards and how members will be appointed/selected. Proposals range from a board with only public members (DRA, CEC Staff, DGS, EMG, the Sierra Club & SCG) to boards that have both voting public members and non-voting private market members. (Coalition)

Common Features in the Administration Function

- All Parties agree that administrative staff should be kept separate from the policy making function.
- All Parties agree that the administrator must work within a budget approved by the board.
- All Parties agree that the administrator should be responsible for procuring energy efficiency services and reporting on program spending.

Key Differences in Administration of PGC Funds

UDC Role -- Parties propose distinctly different administrative roles for the utility distribution company. There are three basic approaches: (1) granting the UDC's a prominent role in administering all PGC programs (SCG & the Coalition proposal); (2) allowing the UDC to bid (subject to certain conditions) for the right to administer these programs (the CEC Staff and DGS proposals); and (3) precluding the UDC from administering any PGC funds (the Sierra Club, DRA, and EMG proposals).

Parties also disagree on the tasks included within the administration function. Some Parties assign primary responsibility to the administrator, with governing board oversight, for developing program designs and delivering certain programs to their customers (SCG & the Coalition). Other Parties assign these tasks to either the governing board (DGS, EMG) or a combination of governing board staff and local contractors (CEC Staff).

Local vs State Administration -- Parties' proposals differ on the level of administration that may be needed for different types of energy efficiency programs. In some proposals UDC's or

local boards are responsible for administering the allocation of services for all program types (the Coalition and SCG), while in other proposals statewide administrators are responsible for regional or national market transformation activities while local administrators are responsible for procuring and implementing local market transformation activities. (CEC Staff, EMG). In other proposals a state level administrator is responsible for administering all types of programs (DGS, DRA, Sierra Club).

Procurement Strategies -- Parties also disagree on the need for the governing board or the Legislature to prescribe how PGC funds will be disbursed. Some proposals give the administrator discretion in determining the best procurement strategy to achieve a given governing board objective (DRA, CEC Staff, DGS, SCG and EMG) while others seek to prohibit certain types of contracts between the Administrator and their affiliates and or build in a specific funding commitment for use in a specific procurement strategy known as the standard performance contract. (The Coalition)

Common Features in the Implementation Function

- All Parties agree that qualified energy service providers from the private market should provide energy efficiency services or equipment to specific customers.

- All Parties agree on the need to develop and operate both local/customer level market transformation efforts as well as participate in a variety of upstream activities such as partnerships with distributors and manufacturers to transform other markets.

Key Differences in the Implementation of PGC Activities

- Parties disagree on who should design and be responsible for implementing state or regional upstream market transformation programs. Candidates include board staff, UDC'S, contractors for the board or director elected boards.

- Parties disagree on whether the program administrator or its affiliates can also be eligible to either bid for or directly provide energy efficiency services in the local market if these activities are funded by the PGC. The Sierra Club, CEC Staff and DRA proposals allow administrators to develop program designs as long as all the actual implementation work is contracted out to the private market. The Coalition proposal would allow affiliates of the utility administrator to compete for PGC funds subject to certain limitations and oversight by the board.

- The proposals also differ on the mechanisms recommended to promote market competition for delivering energy efficiency services. Potential mechanisms in the proposals include the use of standard performance contracts, bidding for specific efficiency services, developing listings of qualified energy service providers, and/or developing proactive customer empowerment activities.

Common Features in the Market Barrier Assessment and Program Evaluation Function

- o All Parties agree on the need to routinely assess program performance towards reducing market barriers or transforming markets and to use this feedback to redesign programs.

- o All Parties agree on the need to verify the energy savings or other targeted program objectives being achieved at both the customer and program level. Responsibility for completing the verification of energy savings varies by proposal and by type of program.

Key Differences in the Market Barrier Assessment and Program Evaluation Function

- o Parties disagree on who or which organizations should perform market assessments to determine if programs have been successful in reducing market barriers or achieving specific market effects. Candidates to perform this function in the proposals include existing state energy agency staff, (CEC Staff, DGS, and DRA) board or governing board staff (DGS and the Coalition), UDC's (SCG), advisory boards to the CPUC (Sierra Club) and director elected boards. (EMG).

- o Finally, Parties disagree on how much staff and resources should be devoted to planning, market assessment and evaluation functions.

CRITERIA TO CONSIDER WHILE REVIEWING ADMINISTRATION PROPOSALS

Most Parties in the Working Group recommend that the CPUC consider the following criteria during its evaluation of the administrative options summarized in the next section. Other Parties (specifically DRA and TURN) cannot support at least some of the criteria listed below and see little value in listing all of these criteria. The majority of the Group decided that including these criteria would serve a useful purpose by providing the CPUC with a potential framework or at least list of issues to consider.

Compatibility with Broader Public Policy Goals

- C Provides opportunities for and facilitates the realization of intelligent customer choice
- C Supports the state's policy commitment to the realization of all practically achievable and cost beneficial energy efficiency
- C Supports market transformation goals
- C Fosters the provision of energy efficiency services by the competitive market
- C Makes the best use of the energy efficiency expertise and resources acquired over the years by utilities, other energy efficiency firms and governmental agencies
- C Promotes the minimization of all costs including administrative, regulatory, evaluation, marketing and customer decision costs

Accountability and Oversight

- C Avoids conflicts of interest between those who allocate and those who receive public funds

- Provides for public overview necessary to assure accountability for the responsible and effective expenditure of public funds
- Avoids unnecessary micro-regulatory entanglement in detailed decisions of energy efficiency service providers or their customers
- Provides for the compatibility of incentives between those who administer public funds and desired public outcomes

Administrative Effectiveness

- Provides opportunities for input and feedback from stakeholders, market participants, outside experts, and customers
- Provides a mechanism to learn from program experience and take action based on the improved understanding that results
- Ensures equity for customers in different classes and local areas, so that those who pay the PGC-funded have sufficient opportunities to receive the benefits of energy efficiency services

Customer Assistance Issues

- Contains a commitment to work towards a more consumer friendly information environment
- Provides for adequate safeguards for customers, quality service for customers, and responsiveness to customer needs, requests, and complaints
- Provides for adaptation to local customer needs and characteristics
- Where appropriate, provides avenues for customers and providers within PGC programs to resolve disputes

Feasibility and Transition Issues

- Can be implemented without undue regulatory or political obstacles to overcome
- Can be implemented by January 1, 1998
- Provides for an effective transfer and smooth administrative transition from today's energy efficiency delivery systems to the new structure
- Provides for a smooth transition to new program designs targeted at directly reducing and overcoming market barriers
- Avoids disruption in the market or a break in energy efficiency services to customers during the transition

SUMMARIES OF THE MISSION, FUNCTIONS AND KEY ISSUES ADDRESSED IN EACH PROPOSAL

The next section provides a summary of each proposal written by its sponsor in this order:

Proposal Name	Sponsor (s)
o The California Energy Efficiency Exchange	Division of Ratepayer Advocates
o The Energy Efficiency Fund of California	Sierra Club
o Consensus Proposal on Energy-Efficiency Initiatives for California's Restructured Electric Services Industry	National Association of Energy Service Companies, Enova Energy, Onsite Energy Corporation, CES/Way, Proven Alternatives, Natural Resources Defense Council, Environmental Defense Fund, Pacific Gas & Electric, Southern California Edison, San Diego Gas & Electric, and The Rocky Mountain Institute
o Energy Efficiency Surcharge Administration	Southern California Gas
o PGC Administration Proposal: The California Energy Efficiency and Public Interest Research Board	California Energy Commission Staff
o Ratepayer Responsible Boards: The California Public Energy Resources Board	Environmental Marketing Group
o Summary of Independent Administration of PGC Funds for DSM	SESCO and RESCUE
o Administration of the Public Goods Charge by an Existing State Agency	California Department of General Services

The California Energy Efficiency Exchange Proposal (sponsored by DRA)

The California Energy Efficiency Exchange (CEEX) represents the institutional framework for the administration of funds collected through the Energy Efficiency Public Goods Surcharge. The CEEX consists of a mixture of public agencies, private/non-profit, and private/for-profit entities. These entities are linked by a set of operating principles that define the roles and responsibilities of each entity in achieving the energy efficiency objectives of the CEEX.

The CEEX consists of four entities, each of which provides a critical function:

- a Governing Board (a public agency, either the CPUC itself or with CPUC representation, charged with policy-setting responsibilities)
- an Independent Administrator for Energy Efficiency (IAEE) (a non-profit, private, organization responsible for the administration and management oversight of PGC funds in accordance with policies set by the Governing Board)
- Customer Protection and Decision-Making (CPUC Staff, implementing Governing Board policies for customer protection for efficiency services)
- Market Assessment (public agency staff, responsible for evaluation activities including the assessment of the market structure and market power in the energy efficiency services industry)

The Governing Board of the CEEX is comprised of either: (a) the CPUC itself; (b) a CPUC-designated board, with representatives from, e.g., the CPUC, the CEC Staff, the Consumer Affairs Department; or © a legislative-designated board, with representatives from the CPUC and other public agencies. The Governing Board will provide a policy-setting function for CEEX activities, much as the CPUC currently does for the utility-administered DSM programs.[11] The Governing Board will select the independent administrator of PGC funds (through a competitive solicitation of bids from non-profit, private, organizations) and provide general policies in the form of allocation guidelines and procurement policies and mechanisms. The Governing Board will also have responsibilities for establishing policies for other elements of the CEEX-- customer protection (in parallel with customer protection issues for energy providers generally) and market assessment (in parallel with assessments of energy industry market structures and market power generally).

The IAEE will be a non-profit, private entity that will administer and manage PGC funds and activities. After selection by the Governing Board, the IAEE will administer PGC funds for the scope of activities determined by the Governing Board and in accordance with the policy guidelines determined by the Governing Board. The IAEE will have its own staff and may have its own Board of Directors. The IAEE board and staff will not include any person with a financial interest in a company that seeks funds administered by the IAEE. The IAEE staff will fully develop specific programs and projects that will assist in the effort to transform energy efficiency markets and create a competitive energy efficiency industry. All funds disbursed by the IAEE, whether in the form of projects that will provide customer-specific assistance or non-customer specific activities to "upstream" elements of the energy efficiency infrastructure, will be allocated under some form of competitive procurement.[12]

[11] Policy-setting" refers to the kinds of statements adopted by the CPUC as the "DSM Policy Rules."

[12] "Competitive procurement" refers to an implementation mechanism that solicits and selects, on a competitive basis, proposals for use of PGC funds by any entity—private, for-profit; private, non-profit; a local government, an individual customer or group of customers, and (if the PGC and CEEX apply to municipal utilities), municipal utilities. The conditions under which a utility affiliate or UDC would be eligible to compete will be determined by the Governing Board.

The two other elements of the CEEX—the Customer Protection and Decision-making, and Market Assessment—will be performed by staff at existing public agencies. The Customer Protection and Decision-making function will be an extension of services and responsibilities similar to those that are likely to be established for Direct Access customers, but with special attention to energy efficiency: information to customers regarding qualified energy efficiency service providers; advanced metering systems and billing procedures consistent with customer information needs for making informed energy efficiency investment decisions; balancing customer privacy rights with the information needs of new and existing market entrants in the energy efficiency services industry. These activities will be administered by staff at the CPUC (and at municipal utilities, if the CEEX is extended statewide).

The Market Assessment element of the CEEX will consist of staff at an existing public agency. The market assessment function includes the assessment of all important aspects of the energy efficiency industry and markets: trends and patterns in energy consumption and energy efficiency measure adoption; the monitoring of market barriers and conditions necessary for market barrier removal; market abuse and market power within the energy efficiency industry and between energy efficiency service providers and energy providers.

Collectively, the functions and activities of the CEEX will replace the current set of arrangements that rely on the utility to provide energy efficiency services to customers, under active CPUC regulation. In its place, the CEEX will create a sustainable competitive energy efficiency services industry capable of providing on-going energy-efficiency services and products to customers without continued PGC funds.

The proponents of the CEEX recommend that: (1) the CPUC adopt the CEEX organization structure and the recommended operating principles after considering the Comments and Reply Comments to the Working Group Report; (2) direct the Parties to reconvene to recommend the next level of details necessary to make the CEEX operational by 1998: (a) revise and replace the current DSM Policy Rules with the recommended operating principles; (b) recommendations on the selection criteria for the IAEE and additional policy guidance on the kinds of competitive procurement mechanisms to be employed by the IAEE; © recommendations on the conditions under which a UDC and/or an affiliate should be eligible to compete for access to PGC funds.

The CEEX represents the “functional unbundling” of the current utility-held “DSM asset,” replacing the utility with an Independent Administrator (private, non-profit) of PGC funds with the goal of creating a competitive energy efficiency services industry that can eventually provide energy efficiency services without continued use of ratepayer funds. During the period of transition toward the competitive services industry, the role of public agency involvement will be limited to several public policy roles—providing policy oversight on, and accountability for, public (ratepayer) funds, support for the nascent competitive energy efficiency services industry, and consumer protection services. These public agency activities should go a long way toward the creation of market-mechanisms that will be able to reduce and remove market barriers to energy efficiency, thereby achieving the more general goal of transforming the markets for energy efficiency products and services.

The Energy Efficiency Fund of California
(sponsored by the Sierra Club)

Mission Statement

Sales of energy efficiency products and services in the competitive market provide California with public goods, in addition to private benefits which accrue to individual customers. The CPUC's proposed PGC is a mechanism to collect the value of these public goods from all electricity customers, in order to reinvest in the businesses which provide the public benefits.

The role of the Energy Efficiency Fund of California is to serve, on a non-profit basis, as the entity which manages the investment of money raised through the PGC in the private market for products and services which improve California's energy efficiency.

The Fund's charter is in the form of a contract with the CPUC specifying:

- Policies governing allocations by the Fund, through qualified financial institutions, to businesses supplying efficiency products[13]
- Which efficiency products are to be supported by Fund activities and the methodology for computing customer savings and public benefits from these products
- Guidelines for establishing program budgets, including administrative costs, and accounting and reporting requirements

Administrative Guidelines

The contract between the Fund and the CPUC also specifies the Fund governance process including a Board of Directors comprised of individuals representing the interests of customers and public policies. No Director shall vote on any decision in which the Director has a direct interest. The contract shall also establish an advisory committee comprised of individuals representing other stakeholders and technical experts.

The Fund does not participate in transactions between customers and sellers in the private market. The Fund shall, however, protect customers by monitoring the performance of efficiency products offered by businesses receiving Fund support, to ensure that these products perform satisfactorily, are not misrepresented, and provide the public goods values claimed. Fund support is not available for research or development projects ("upstream market transformation") without explicit direction from the CPUC; pilot projects may be supported by the Fund as part of its market research function.[14] Fund support is not available to for-profit organizations which are exempt from anti-trust laws.

Fund decisions are the responsibility of the Fund's Directors. The Fund has no obligation to compensate any individual for revenues lost as a consequence of Fund decisions which were made in accordance with the guidelines established in the contract with the CPUC. Any affected party may appeal a decision by Fund staff, consultants, contractors, or businesses receiving Fund support to the Directors. Decisions by the Directors may be appealed to the CPUC but only on the grounds that the Fund has violated its contract with the CPUC.

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[13] By efficiency products we mean goods and services which reduce customers' use of electricity and natural gas.

[14] We assume that product development will be supported by a separate RD&D administrator, unless the CPUC chooses to also assign this function to the Fund.

Administrative Functions

The Fund has sufficient staff to achieve the Fund's objectives, but relies whenever possible on outside consultants and contractors to perform administrative services such as fiscal management, program planning, contract management, product evaluation and other technical services, etc. The gas and electric utility distribution companies may offer these services to the Fund on a competitive basis, but the Fund is obligated to choose the best qualified providers.

Programs and budgets to support businesses providing efficiency products and services consistent with CPUC guidelines shall be adopted annually by the Directors and submitted to the CPUC for approval or modification. Programs shall be designed to support businesses servicing all market sectors, through "standard offer" mechanisms whenever feasible. Programs also shall include dissemination of appropriate public information and technical assistance for the private sector. The primary criterion for Fund-supported programs shall be the reduction in use of electricity and natural gas by customers of the jurisdictional utilities, consistent with equity between market sectors.

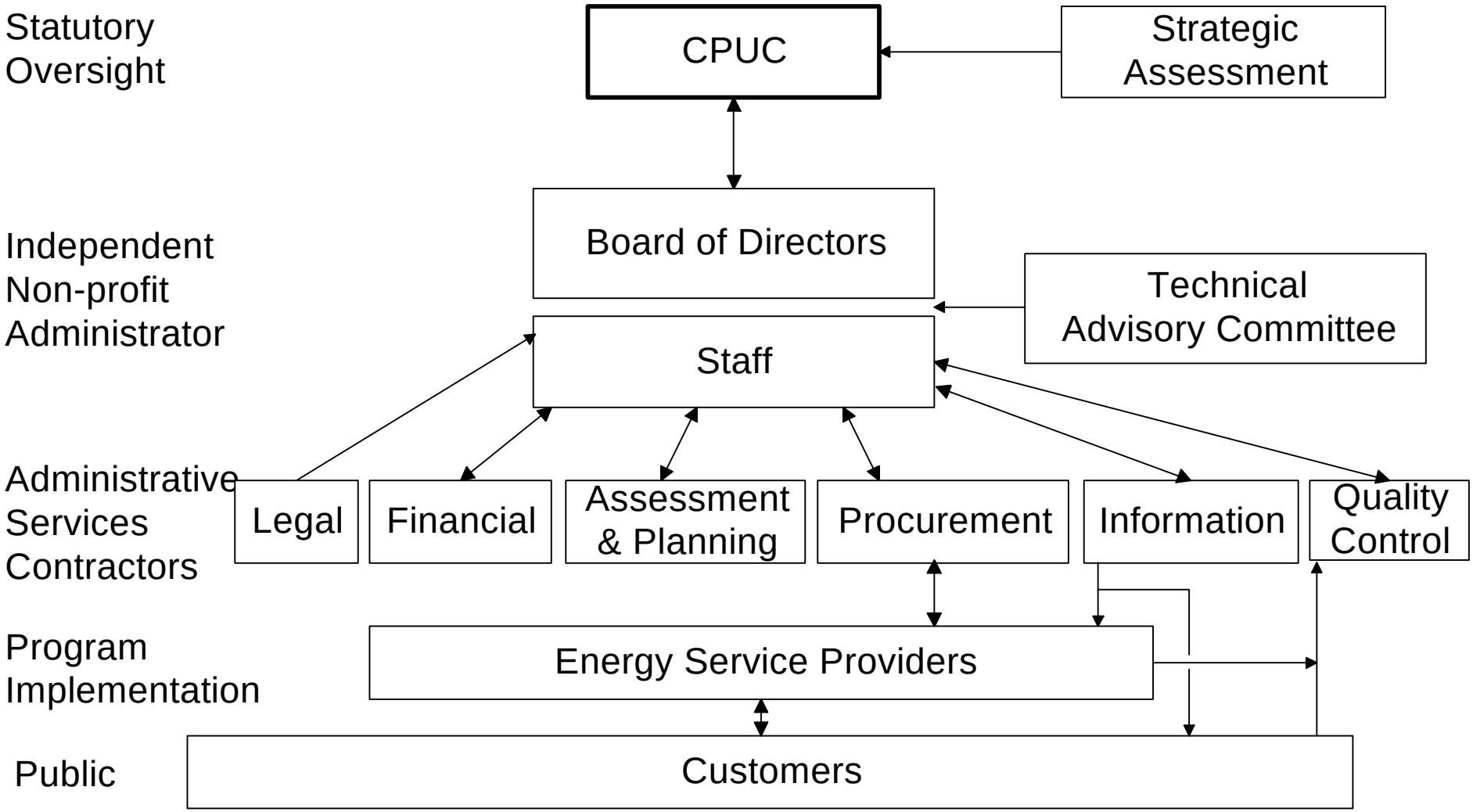
It is estimated that administrative costs will be less than 10 percent of total PGC energy efficiency funds, and that costs incurred by the Board and Fund staff will be less than 10 percent of total administrative costs.

Unique Characteristics. Present delivery mechanisms rely on the monopoly utilities, regulated by the CPUC to control costs and minimize financial conflicts of interest between energy sales and conservation. Efficiency products are considered monopoly utility resources whose costs are included in rates.

The advent of competitive electricity markets makes the present delivery mechanism obsolete. The PGC acknowledges that efficiency products provide *public* goods to *all* customers, whether they purchase energy from the utilities or not. In a competitive environment, efficiency resources must belong to everyone, not just the utilities. In addition, utilities remaining in the generation business have an inescapable conflict with the growth of competitive efficiency markets. While this conflict might be minimized by giving sufficient "incentives," they serve to protect the utilities from the very competition the CPUC has pledged to nurture. Furthermore, experience has shown that such incentives are exceedingly expensive and unreliable.

Administration of the PGC by the Fund, a state-wide non-profit entity which is independent from all market participants, avoids all conflicts of interest. It allows the utilities or their affiliates to compete in the competitive market, subject to resolution of market power concerns by the CPUC as specified in the Fund's contract. Standard offer program design limits interference by the Fund in market transactions. By contracting for administrative services, the Fund ensures that utility expertise is retained at least cost. A fixed term contract and limited staff avoids the development of a large entrenched bureaucracy.

Independent Administration
of
PBC Energy Efficiency Funds



CONSENSUS PROPOSAL ON ENERGY-EFFICIENCY INITIATIVES FOR CALIFORNIA'S RESTRUCTURED ELECTRIC SERVICES INDUSTRY
(Sponsored by the Coalition)

Overview

The goal of this proposal is to foster a robust and sustainable energy efficiency(EE) marketplace in California by overcoming market barriers and maximizing the demand for and adoption of technologies and services with energy savings capabilities.

The proposal envisions the use of a public goods charge (PGC) on electric distribution service to (1) underwrite energy efficiency investments and other activities aimed at removing market barriers to and increasing attainment of cost-effective energy savings in all markets for all customer classes and (2) stimulate the development of more competitive energy service markets.

The CPUC will retain ultimate authority over program budgets and implementation. Subject to CPUC approval, a new statewide Energy Efficiency Board will establish guidelines for administration of PGC funds by utility distribution companies (UDC), which will serve subject to Board oversight.

The Energy Efficiency Board (Board)

The CPUC will appoint the Board composed initially of nine voting and six nonvoting members with staggered terms of 2 or 3 years. The CPUC will approve conflict-of-interest rules to govern deliberations and voting of members.

The Board's functions will be to (1) develop guidelines applicable to the use of the energy efficiency portion of the PGC funds, (2) solicit and review proposals by UDCs and others regarding UDC administered program budgets and implementation, (3) provide policy guidelines on the development and revision of evaluation and verification protocols, (4) report to the CPUC on all energy efficiency-expenditures and results, and (5) assist independent reviews (at least once every three years) to assess the Board's effectiveness, efficacy of program guidelines, and UDC compliance with the Board's guidelines.

The Board's budget will be established by the CPUC at an amount not to exceed one-half of one percent of the energy efficiency portion of the PGC. Subject to final CPUC approval, the budgets and contents of initiatives will be determined through annual plans created by UDCs with input from other market participants and stakeholders, and approved by the Board. Approved plans will be submitted to the CPUC by advice filing while areas of conflict will be handled through an expedited decision process at the CPUC. UDCs will report program results and will apply approved measurement and evaluation protocols.

Standard Performance Contract Competitive Markets

A new standard performance contract program is an important element in achieving the goal of this proposal to foster a robust and sustainable energy efficiency marketplace. Payments will be based on posted prices for saved electricity with the understanding that the price and other terms may be varied with Board approval at monthly or other intervals. Initiatives will target the elimination of market barriers to cost-effective retrofit opportunities in the commercial, institutional, and industrial sectors. Funds unspent in the initial three years may be used for later years.

A goal of the Board should be statewide uniformity where appropriate in standard performance contract conditions, including those governing threshold qualification for awards, posted prices, and measurement and verification procedures. The CPUC should promptly convene a design committee to allow interested parties to seek an early and timely consensus on specific provisions of the first standard performance initiatives.

Other DSM Programs

UDCs may propose other approaches for markets to which standard performance initiatives may be ill-suited or premature. These will be designed to prevent conflicting with, confusing, or disrupting standard performance markets. If standard performance programs are unable to benefit segments of the program's target

market, UDCs may propose alternative service delivery mechanisms for Board consideration. The UDCs will actively pursue opportunities to competitively outsource services associated with other programs.

Innovative and Broad Scale Market Transformation Initiatives

In consultation with all interested parties and the Board, UDCs collectively will propose for Board approval energy-efficiency programs and budgets to transform California markets through mechanisms that coordinate the efforts of multiple parties, including initiatives of nationwide scope, and pilot tests to achieve sustainable reductions in market barriers.

UDC Incentives

The Coalition supports a new performance-based shareholder incentive mechanism to be administered by the Board subject to CPUC review. Reward/penalties will be based on (1) cost-effective administration of PGC funds, (2) expansion of the range, diversity and quality of services available to customers through independent providers, and (3) delivery of cost-effective savings that reflect market transformation.

Current CPUC policy ensures there is no linkage between utilities' recovery of fixed transmission and distribution costs and their retail kilowatt-hour sales. Although the specific mechanism may change as restructuring proceeds, this issue must be addressed for UDCs to avoid conflicting incentives.

The Role Of UDC Affiliate

If UDC affiliates secure contracts accounting for 15% of a year's standard performance contract funding within their own UDC's service territory, any additional funding will require a Board recommendation and CPUC finding of no market power abuse. The Board will establish procedures for interested parties to submit complaints about and secure prompt resolution of any violations of affiliate guidelines. Further appeal will be available to the CPUC. The Board will reevaluate these limits following two years of experience, in consultation with all interested parties.

Proposed Transition Schedule

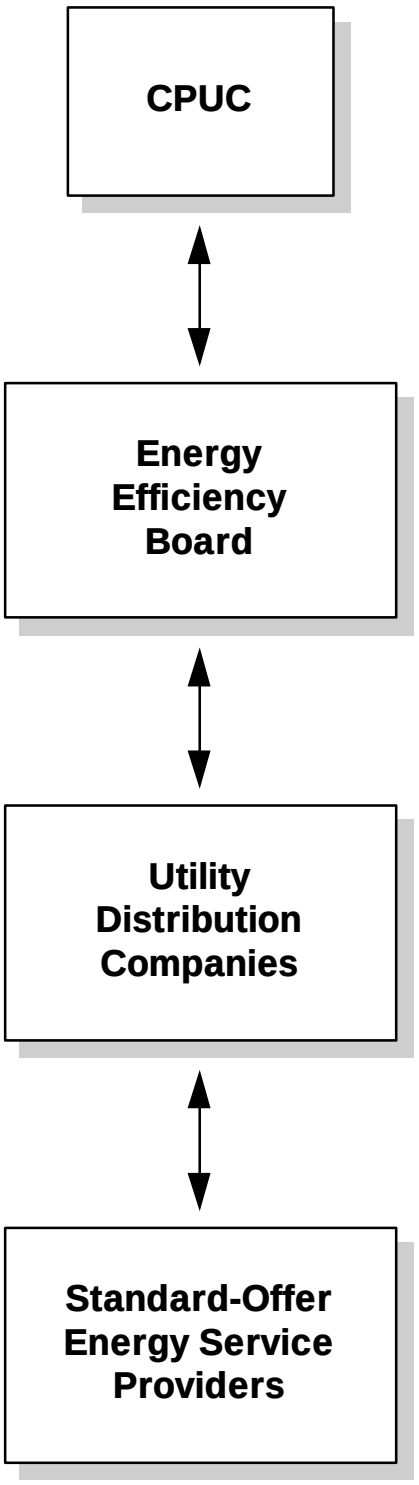
The proposed schedule calls for full-scale implementation in January 1998. The schedule assumes (1) design committees are convened in September 1996, (2) the CPUC approves the new structure and appoints Board representatives in January 1997, (3) the Board recommends guidelines in March 1997, (4) the CPUC adopts final guidelines in June 1997, (5)CADMAC recommends revisions in measurement and evaluation protocols in June 1997, (6)UDCs submit proposed 1998 initiatives and budget allocations in September 1997, and (7) the Board forwards its recommendation for action on UDC proposals to the CPUC.

Key Features

This proposal can be implemented by January 1, 1998, with a smooth transition that will not disrupt the market or cause a drop in the availability of energy efficiency services to customers. It meets the CPUC's objectives by providing independent administration through the Energy Efficiency Board, utilizing the expertise of existing infrastructures through the UDC's administrative role, and fostering the growth of the competitive market through standard performance contracts. It also allows for unique regional needs to be addressed, while providing statewide oversight and consistency. There is no need to establish a new bureaucracy, and accountability is explicitly addressed since energy efficiency implementors (Energy Services Providers and UDCs) are under Board and CPUC oversight. There are sufficient avenues for customers, energy service providers, and other stakeholders to have their concerns addressed by the Board. The proposal also protects for potential market power or self dealing concerns through its limitations on UDC and affiliate activities.

Coalition Proposal on Energy Efficiency Initiatives

For California's Restructured Electric Services Industry



- Ultimate authority over program budgets and implementation
- Set budgets
- Appoint EE Board representatives
- Approve budgets and program plans
- Rule on conflicts
- Approve standard-offer structure

- Develop guidelines for administration of PGC funds and recommend for CPUC approval
- Recommendations on UDC program plans and budgets for CPUC approval
- Report to CPUC on expenditures and results
- Provide policy guidelines to CADMAC on evaluation and verification protocols

- Develop program plans for Board review
- Administer PGC funds and Standard-Offer programs
- Develop Core DSM programs
- Propose upstream market transformation initiatives for Board approval
- Report results to the Board

- Provide implementation of energy efficiency services through Standard-Offer and Core programs
- Provide input for creation of UDC program plans and market transformation initiatives

Energy Efficiency Surcharge Administration
(sponsored by Southern California Gas Company)

This document outlines SoCalGas' position on the proposed administration and allocation of gas energy efficiency surcharge funds by an independent, centralized administrative authority.

While SoCalGas strongly supports the continuation of utility energy efficiency efforts, we are deeply concerned about the additional customer costs and loss of current administrative efficiencies of a new, centralized, statewide energy efficiency administration function. We are certain that gas customers will suffer increased administrative costs, as a portion of total energy efficiency efforts, is a statewide independent administrative function is implemented. It is also likely that administrative effectiveness will decline as currently applicable utility shareholder incentives for efficient administration are removed and the administrative function becomes more bureaucratic and geographically divorced from energy efficiency program delivery sites.

Administrative costs will rise relative to current levels with an independent administrator. Less than 10 percent of SoCalGas' energy efficiency funds are currently spent on program administration. If an independent administrative function is created for gas energy efficiency programs, start-up costs and duplicative efforts will raise the cost to deliver and administer energy efficiency services to our customers.

An independent surcharge administrator may not have appropriate incentives to be efficient. Utility shareholders currently bear the risk of poor delivery and performance of energy efficiency programs through the shareholder sharing mechanism. In addition, customers can seek redress from regulators. This system provides very effective checks and balances to assure that utility customers receive value for the expenditure of funds on energy efficiency programs. An independent, non-profit energy efficiency administrator would bear no comparable financial responsibility.

Preferred Organizational Option: Utility Distribution Company Administration

SoCalGas is certain that the most efficient administration of surcharge funds will be accomplished using existing utility distribution company organizations, in combination with established oversight functions of the CPUC. Decision-making and program delivery to customers will be expedited using existing utility energy services and currently effective regulatory structures, i.e., the annual CPUC advice letter filings, general rate case proceedings and DSM advisory committees, will assure the proper oversight of gas utility energy efficiency programs.

Utilities should be incented to deliver a higher percentage of energy efficiency programs through third party procurement efforts. To facilitate the market transformation of energy efficiency services to market-driven energy efficiency service companies, procurement of third party services should be increased using the existing utility procurement infrastructure. Current shareholder earnings should be modified to provide the proper incentives to utilities to transform the energy efficiency delivery channels from mostly utility delivered to market-driven energy service companies. Applying the existing utility systems would reduce the administrative costs of delivering energy efficiency services by employing existing contract review, accounts payable, and credit checking functions that must be maintained within each utility. Existing consumer protection and customer assistance functions would also be employed. The consumer protection and customer assistance functions are most ably performed by a local presence with existing knowledge of the customer base and their region specific concerns, particularly regarding construction activity that would accompany many energy efficiency efforts.

Selection of alternative service providers should be required, in cases where the utility distribution company fails to provide adequate energy efficiency services or opts not to provide such services. Selection of service providers should be governed by a formal bidding process. The specification of an objective, concise, and fair bidding process for energy efficiency surcharge funds can be quickly developed in conjunction and cooperation with the current DSM advisory groups. The bidding process, once codified and approved by the CPUC, should be open to all bidders including, but not limited to, energy service companies, municipal utilities, investor-owned utility distribution companies, unregulated affiliates of utility distribution companies, and utility customers. Bids should be evaluated on a set of measurable criteria aimed at maximizing the value of energy services to customers.

SoCalGas supports third party access to energy efficiency funds that meet customer needs and enhance customer satisfaction. A bidding process, focused on maximizing customer benefits, should be open to all qualified energy service providers, including regulated utility distribution companies and their affiliates. It is efficient and reasonable to allow utility energy service providers, who have the most experience in providing energy efficiency programs, to bid for and provide energy efficiency services to their customers. This will assure that the service providers most knowledgeable about local customers' energy efficiency needs will be allowed to continue to meet those needs.

Existing performance-based financial incentive mechanisms should be continued with modifications to encourage utilities to use third party energy service companies for program delivery to customers. With proper modification, these existing mechanisms will ensure that utilities continue to support cost-effective energy efficiency efforts by providing a fair and competitive return on DSM investments while providing additional opportunities to transform the market for delivery of energy services to market-driven energy service companies. The current financial incentive mechanisms also foster careful program planning and implementation by placing utility shareholders at risk for energy efficiency programs that do not benefit utility customers. The financial incentive mechanisms provide the potential for superior returns from extraordinary performance and shareholder penalties for poor performance. They provide the appropriate incentives for effective program administration.

In conclusion, SoCalGas firmly believes that the current gas utility managed energy efficiency program administrative structure, with appropriate shareholder incentive mechanism modification, is the most cost-effective and customer-responsive energy services delivery channel.

PGC Administration Proposal: The California Energy Efficiency and Public Interest Research Board (CEEPIRB)

(Sponsored by the California Energy Commission Staff)

Mission Statement

The primary mission of the California Energy Efficiency and Public Research Board (CEEPIRB) is: ***to achieve long-term societal benefits by engaging in market transforming and RD&D activities not naturally provided by competitive markets, thereby increasing the range and use of energy efficient products and services***.

Basic Strategy

The basic strategy underlying CEEPIRB-directed programs is a focus on sustainable transformation of markets through reductions in market barriers; a dramatic shift from the current focus on influencing individual customer purchase decisions through financial incentives. This approach is consistent with CPUC policy direction in Conclusions of Law 82, 83, and 84 (D 95-12-063, p. 213).

Principles

The CEEPIRB proposal is based on principles, shown in the long version of the proposal in Appendix A, covering the governing board, administration, program design and the transition. R&D principles will be included when the working group reports are integrated. The principles allow for a range of options for transition and initial administrators.

Transition

Successful market transformation programs will be developed through pilot tests, as subsidy programs are phased out, and market transformation programs are phased in at statewide and local levels. Current utility administration would be subject to an open competition among organizations (e.g.: UDCs, cities, non-profits) that meet qualifications, have capability in place, and can adapt to the shifting program emphasis. Routine reliance on utilities would gradually end. Once a mission, guiding principles, a governing board, and board staff are established, the transition to new administrators could take a variety of paths, and could incorporate portions of other proposals, or be left to the Board to decide upon within guidelines.

Governing Board

The CEEPIRB is governed by a strong statewide board that sets policy guidelines for competing local administrators and guides market transformation initiatives and public interest R&D. The board governs expenditures of public funds, and should therefore be a public agency; a likely candidate is a Joint Powers Authority (JPA) comprised of existing energy agencies. Municipal utilities could join a JPA structure prior to any legislation to establish a statewide PGC. The board must be able to control PGC funds within guidelines, in order to have competitive local administration. The board would direct and receive assistance from a small, strong staff, whose responsibilities are described in the next item. A strong statewide board and staff provides stability and accountability and fosters uniform statewide policies and guidelines.

Guidelines & Strategic Assessment

The board would be assisted by a strong but small staff with responsibility for developing policy guidelines for local administration, managing audits of administrators, and developing and managing pilot tests of new statewide and local market transformation initiatives. Successful programs would be contracted out or "catalyzed" to the best administrative options, so that board staff keeps a strategic focus and avoids entrenchment.

RD&D and Upstream Market Transformation

Public interest research and development and upstream (statewide or nationwide) market transformation programs are more efficiently initiated from a statewide perspective under policy control from the governing board. RD&D functions, which include research on both technologies (generation and end use) and market barriers, will be more completely described during the integration of R&D and EE working group reports. Upstream market transformation initiatives include programs that work with manufacturers, distributors, associations, and other participants to reduce market barriers to energy efficiency, and programs that assist consumers on a statewide basis, such as equipment labeling programs, service provider certifications, and changes in state laws and codes.

Consumer Assistance and Protection

These market transformation activities should be administered at a local level, close to the consumers making energy efficiency decisions, under guidelines from the board. Local administrators would implement new, pilot-tested program concepts developed by strategic assessment. The essence of this function is providing trustworthy information in a friendly, low-transaction cost fashion. One strategy to pilot test is developing independent quality ratings of energy service providers (ESPs) which would be furnished to administrators, and made readily available to consumers. Another is changing bills to make it easier for consumers to make more informed choices about and verify savings from energy efficiency investments.

Provider & Trade Ally Services

These market transformation activities should be administered at a local level, close to the providers that interact with consumers, such as architects, developers, and service contractors. Local administrators would implement new, pilot-tested programs, developed by strategic assessment. The essence of this function is to assist energy efficiency providers and trade allies in trustworthy, current, and competent delivery of energy efficiency products and services. One example is training architects and building contractors in the use of and value of energy efficient design and construction.

Procurement

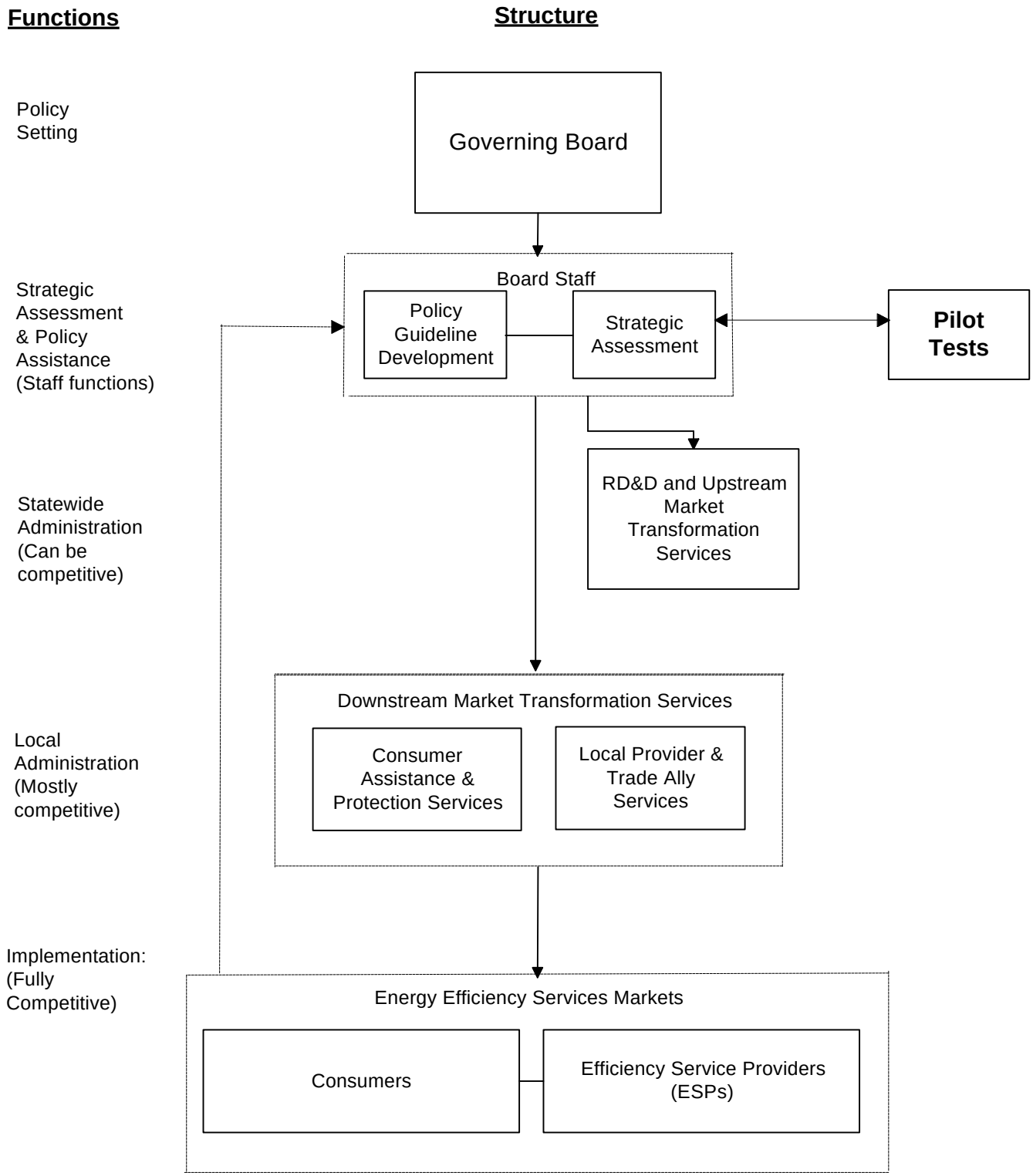
Procurement should be handled by qualified local administrators until subsidies are phased out, with the CEEPIRB board standardizing terms to provide a stable and consistent statewide structure for procurement from ESPs. Procurement administrative costs will be limited by the standard guidelines, and should take no more than 5 percent of the funds allocated to procurement. After the transition, procurement through incentives may be combined with other strategies to increase the overall effectiveness of market transformation plans. The procurement function is not reflected in the flowchart because it is not clear that it will be a significant separate function after the transition.

Unique Characteristics

The CEEPIRB proposal is consistent with CPUC policy direction by reducing reliance on subsidies and placing policy emphasis on the development of market transformation designs that work. CEEPIRB avoids shocks to and captures expertise of the energy efficiency industry by gradually tapering off existing administration and subsidy programs and shifting to new, pilot-tested administrative structures and activities. CEEPIRB includes a variety of flexible administrative options to fit the specific functions of any market transformation programs developed. CEEPIRB allows the efficiency forces of competition to operate to the maximum extent reasonable. Finally, CEEPIRB integrates energy efficiency and RD&D public goods program in one board, and sets the stage for municipal utility participation.

Administering The Public Goals Charge (PGC)

The California Energy Efficiency and Public Interest Research Board (CEEPIRB)



RATEPAYER RESPONSIBLE BOARDS: THE CALIFORNIA PUBLIC ENERGY RESOURCES BOARD (CPERB) (Sponsored by Environmental Marketing Group)

The Independent Administrator (IA): The CPUC's Policy Decision calling for an Independent Administrator of Demand-Side Management (DSM)/Energy Efficiency (EE) program funding did not distinguish between policy and administrative functions. The complexities of EE program governance, design and implementation, require separation of powers and functions. Ratepayer Responsible Boards (RRBs) is a framework for EE programming that avoids overweening regulatory control, in the spirit of devolving electric services to market forces. The CPUC will maintain oversight on key aspects, but the goal of a restructured EE program should be to minimize CPUC responsibilities for EE market development.

The IA will be relatively policy-neutral, being instead a transaction-execution office initially appointed as a Trustee-IA by the CPUC, and later contracted by the CPERB. The IA will receipt all surcharge funds from utilities, manage all associated financial accounts including CPERB and Local Board internal accounts, and supervise all computer systems. The IA will have a Contracts Office to support the RRBs in drawing technical forms and contracts. The IA will efficiently execute all financial disbursements per program requirements, with minimal policy interpretation.

Governance. The CPUC will initiate a reformed EE market program, defining how customer classes are represented and served, and setting budget targets and equity formulas for the surcharge. However, the RRBs will control program design and implementation of the new EE "franchise", including ownership and control of assets by Local Boards. While program authority will be bound up in the two levels of elected Boards, a Regulatory Oversight Office (ROO) will provide consultation as well as exercise specific CPUC oversight authority. The ROO will communicate with municipal utilities to coordinate the CPUC EE policies. Such coordination by means of MOUs will create a unified California EE market.

Initially, the CPUC will appoint Trustee-Directors for Local Boards during Stage I. In Stage II the Local Boards will be elected by ratepayers with a simple ballot method. Election campaign conduct will be governed by bylaws, internal Board policies and rulemaking as needed. Initially, Local Board Districts will conform to existing UDC boundaries. Localized Districts will evolve as the industry restructures, with a petition process to the CPUC providing the due process mechanism. A conservative evolutionary path utilizing the ROO to study boundary petitions is preferable.

The Directors selected at the UDC/LDC level will in turn elect the seven state CPERB Directors, comprising a "superboard", i.e. Director-Elected Board (DEB) in Stage II. The CPUC will initiate the CPERB by appointing Trustee-Directors in 1997. The CPERB will develop unified EE program policy, but be accountable to Local Boards and local market realities. The CPERB will accept technical standards and monitor technological trends in consultation with the ROO. The CPERB will contract for the operator(s) of the IA Office in Stage II. Subject to CPERB approval, the IA procures all information systems and financial services. The California DGS could function as a single centralized IA during Stage I on an appointive Trustee basis. If this occurs, the DGS' orientation should be to obtain vendor contracts with financial

intermediaries, claims-processing organizations, and technical support for the RRBS, such that DGS exits program administration responsibilities at Stage II. The CPERB will have dominant program design authority, but Local Boards will possess substantial discretion, including authority to prioritize programs and exercise budget shifts, initiate pilots, and incentivize managers, Facilitators, EEPs, and ESPs.

The ROO will carry out review functions that are best contained in a specialized CPUC office. Because of initial program change, the ROO must be pro-active on many issues, but it is essential the CPUC clearly define the ROO functions in its Decisions, to avoid confusion of its functions with the RRBS. ROO functions will include managing transfer of certain information assets from UDCs, for use by emerging ES industry segments. The ROO will be the intervening CPUC agent in any disputes between the CPERB, the IA, and UDCs. The ROO will act as an Inspector General as the CPUC deems necessary, establishing reporting standards and procedures, and reviewing audits of the CPERB, Local Boards and IA. The ROO will conduct REB boundary studies and supervise REB and CPERB elections. The ROO will participate in MOUs with other State agencies, municipal utilities, IOUs and local jurisdictions.

The California Energy Efficiency Exchange (CEEE). The RRB Proposal proposes that different customer classes have different EE program participation mechanisms. Local Boards and the CPERB will be oriented to residential interests. A CEEE will be the intermediary for CIAI classes. It will be more private in nature than the REBs and CPERB. The CEEE will intensively pursue information-based and market-based methods of transacting EE goods and services.

Accountability. The RRB structure provides the checks, balances and separation of functions needed for a complex program. Customer-based Boards possess legitimacy that will put to rest the current conflicts over DSM/EE programs. Resiliency of policy formation is inherent to a layered Board design, which will be more responsive to California's large diverse market. Conflicts-of-interest of Board directors can be managed as stringently as the CPUC deems reasonable. The ROO addresses the basic need for accountability.

Feasibility and Transition Issues. Retaining existing IOU boundaries for startup of Local Boards simplifies the transition. The corporate form of RRBs promotes efficient management. Quality of Boards will depend on compensation standards and method of executive search. RRB directors should be full time working directors. The RRB model is operationally compatible with the existing municipal utility industry. Establishing election machinery is not an unreasonable obstacle. The CPUC should appoint Trustee-Directors to accomplish incorporations, with subsequent election provisions provided for in corporate bylaws. A Stage I and Stage II process is set forth for phasing organization. The CPUC should designate key Advisory Committees and award necessary consulting contracts early in 1997 to enable the new Boards to be operating by July 1, 1997. The issue of political will is central to issues of feasibility. The CPUC must act decisively for a new basis for the EE/ES industry to roll out. Existing EE "infrastructure" currently associated with utility supervision will move with the CPUC's decision. Some utility-supervised programs in the CIAI classes can be integrated into the CEEE. Limited funding can be considered for a one-year phaseout period for some utility-supervised ESCO contracts, but the shift to a new EE market structure should be underway by January 1, 1998.

FIGURE 1

RATEPAYER RESPONSIBLE BOARDS

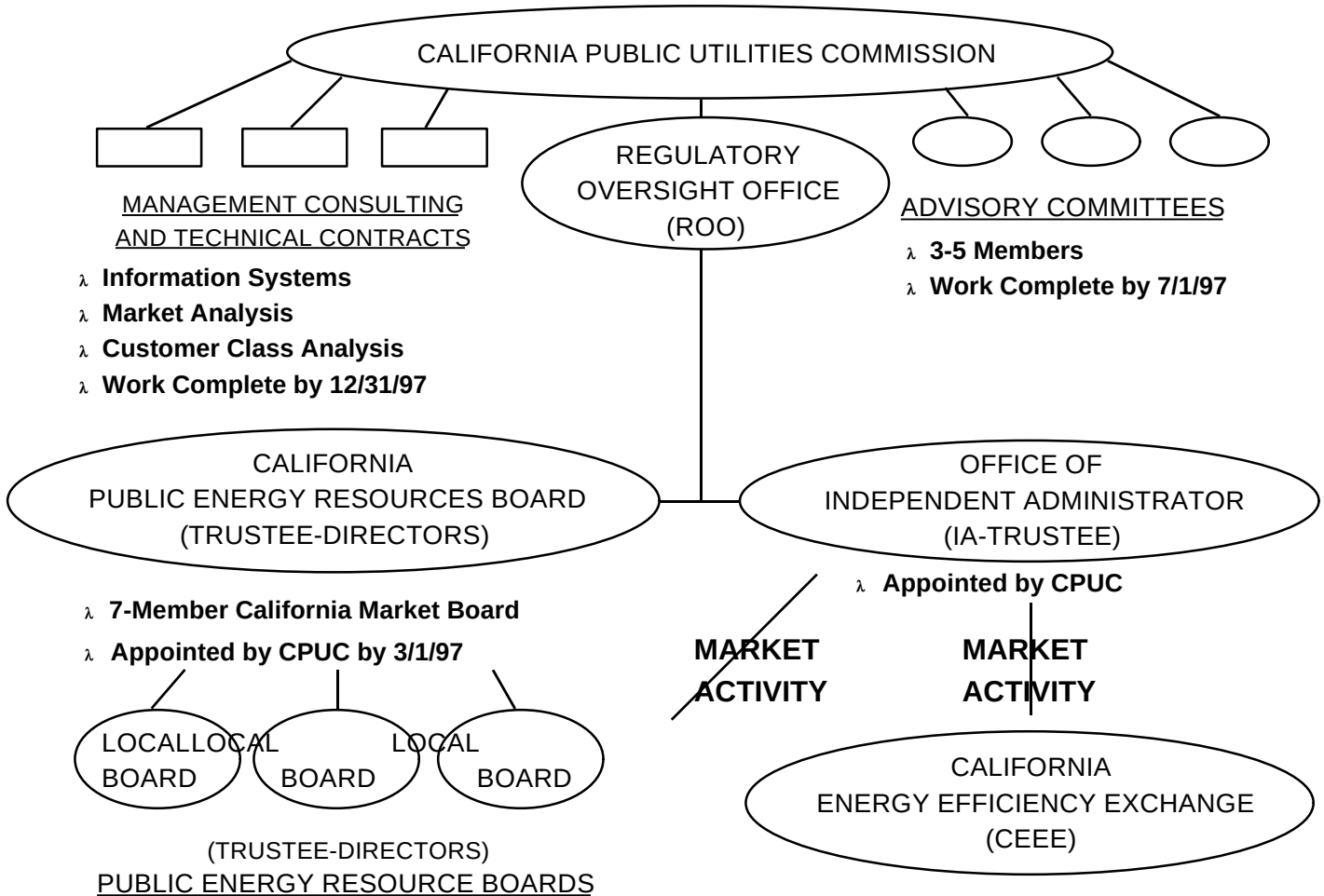
STAGE I: JANUARY 1, 1997 - FEB 29, 2000

REGULATORY DECISIONS

1997 INITIATING ACTIVITY

POLICY & GOVERNANCE (GLOBAL BUDGET AUTHORITY)

MARKET-SERVERS (DISCRETIONARY BUDGET AUTHORITY)



SUMMARY OF INDEPENDENT ADMINISTRATION OF PGC FUNDS FOR DSM
(sponsored by SESCO and by RESCUE
--Residential Energy Service Companies' United Effort)

The most important DSM-related decision for the CPUC is how to structure the administration of DSM surcharge-funded activates, as their ultimate effectiveness will depend on the efficiency and motivation of those administering the funds collected through the Public Goods Charge (PGC). The RESCUE/SESCO proposal is based primarily upon DRA's proposal and incorporates elements offered by the Department of General Services (DGS), Sierra Club, and CEC Staff.

Policy Setting. A **Governing Board (GB**) of public officials would set policies for use of PGC funds dedicated to energy efficiency, including low-income weatherization. Unless utilities other than the CPUC-regulated utilities participate, the **GB** would consist of CPUC designees. If the publicly-owned utilities also participate (due to legislation), the **GB** could be the California Alternative Energy and Transportation Financing Authority or similar board. **GB** officials would be subject to the financial disclosure and conflict of interest rules applicable to government officials. The **GB** would hire its own small staff, while DSM policy staffs of the CPUC and CEC could be reduced. This differs from the DRA proposal, which envisions a GB using the staffs of other state agencies.

Independent Administration. The **GB** would conduct competitive bidding to select several **Independent Administrators (IAs)**, with at least two operating in each part of California. At least one of the **IAs** would operate statewide and handle upstream market transformation activities. Having several **IAs** operating statewide would better enable the **GB** to use competition to assess their relative performance. If there is only one **IA** per utility service area, evaluation will be more difficult and subjective. The **GB** would assess the relative performance of the **IAs** and focus PGC funds on the more effective **IAs**, while maintaining at least two (preferably more) **IAs** operating in each part of California.

Bidders could include nonprofit entities, government agencies (such as DGS), and for-profit companies not affiliated with a regulated electric or gas utility. Instead, utility-affiliated companies and ESCOs would compete with all other for-profit and nonprofit corporations to perform DSM projects (see **Program Implementation** below) and thereby utilize their DSM expertise without subjecting PGC fund administration to conflicts of interest.

DGS could be a potent bidder and effective administrator but should be subject to competition and a limitation of the percentage of PGC DSM funds devoted to improvement of DGS-owned or operated buildings. Utilities and their affiliates would not be eligible to administer DSM PGC funds, because they would have anti-competitive advantages in their opportunities to (1) cross-subsidize **IA** activities (allowing low-ball bids to undercut competitors); (2) recoup funds by selecting themselves or other utility affiliates to perform the DSM work, despite bids from more efficient service providers; (3) direct expensive DSM activities to certain customers in order to persuade them from seeking other energy suppliers, thereby concentrating DSM funds on customers most able to take advantage of retail wheeling (industrial and large commercial), to the detriment of residential customers; (4) direct effective DSM activities to reduce the loads of customers that have already taken advantage of retail wheeling in order to reduce the revenues of other energy suppliers (again concentrating DSM funds on large usage customers); (5) fund less effective (or hard to verify) DSM activities in their own service areas.

Further, with non-utility affiliated **IAs** there would be no need for ERAM-type "lost revenue" recovery mechanisms, as the **IAs** would not suffer any "lost revenue" due to the effectiveness of DSM activities and would not face the conflicting motives facing a utility-affiliated **IA**.

All IA board members would be subject to financial disclosure and conflict of interest rules similar to those for government officials. A financially self-interested **IA** board of "DSM stakeholders" could compromise the use of PGC funds for DSM by the specter of mutual back-scratching and implicit deals by board members to obtain funding for their own projects or relaxed M&E of their projects.

Program Implementation. The **IAs** would use standard offers and "pay for performance" competitive bidding to enable private firms, including utilities and their affiliates, to implement DSM projects. The **IA** would periodically establish a "market transformation price" for electricity and gas savings for each customer class and would pay any qualified energy service provider (**QESP**) that price for *ex post* measured and verified energy savings from the **QESP**'s programs implemented after that time. The price and program would be adjusted to encourage greater efficiency, with a price consideration for the comprehensiveness of the energy conservation treatments, to discourage creation of lost-opportunity DSM.

The important features of a "standard offer" system for obtaining energy savings, based on experience to date in New Jersey, include: (1) a pre-set price per kWh or per therm saved (differentiated by time, season, and customer category; (2) an "open" continuing solicitation for new projects from **QESP**s and customers; (3) standardized contracts and procedures for billing, payment, access to customer data, etc.; (4) pre-specified, public M&E protocols for use by any **QESP**, with an approval process to add new M&E protocols; (5) responsibility of the **QESP** to pay the administrative costs specific to the **QESP**'s program or project, so that its overall cost-effectiveness can be accurately judged.

The statewide **IA** might achieve "upstream market transformation" by contributing to international, national, or state-level projects, subject to evaluation of such efforts for effectiveness. All programs would be required to compete for funding on the basis of overall cost-effectiveness, fully considering "market transformation" effects. Since "market transformation" should result in greater savings per dollar invested, it will have a natural advantage in offering the most "bang for the buck."

Existing utility DSM programs should be closed out at the end of 1997. The balance of the DSM bidding pilot contracts, which extend into 1998 and beyond, should be transferred to an **IA** for administration.

The profits for any company (including any utility or affiliate) implementing a PGC-funded DSM project would be included in the bid price or in the standard offer price. Thus, there would no need for the CPUC to continue the "DSM shareholder incentive" mechanism.

Consumer Protection and Decision-Making

This would be the responsibility of the **GB** and its staff, which would: (1) compile and distribute information to consumers on DSM opportunities and the performance of **QESP**s; (2) furnish to **QESP**s disaggregated customer usage data to enable efficient marketing of services and measurement of results, thereby increasing the ability of the private sector to provide cost-effective DSM services to customers with lesser use of PGC funds; (3) coordinate use of the utility billing systems for collection of QESP charges to customers, helping to overcome the "first cost" barrier to customer investment in DSM.

Market Assessment

The **GB** staff would be responsible for measurement and evaluation (M&E) of the performance of the **IAs**, and their contractors, using protocols building upon those already adopted by the CPUC and by ASHRAE. The **GB** would develop a stable of independent M&E verification experts.

Proposal for Administration of the Public Goods Charge by an Existing State Agency -- Department of General Services

This proposal describes how the Public Utilities Commission (CPUC) may make use of existing state resources to administer the Public Goods Charge (PGC) funds. By contracting with the Department of General Services (DGS) to administer the funds and operate the program, the CPUC will retain control of the various policy aspects of the program, while handling the actual administrative and operational aspects in the most expeditious, cost-effective, and flexible manner possible. The California Energy Commission (CEC) and other stakeholders will continue to have significant input on the policy aspects of the use of the funds through the Public Energy Goods Board, also bound by contract to the CPUC.

The essence of the proposal is as follows:

- The CPUC would appoint a Public Goods Energy Board ("the Board") consisting of 3 members appointed by the CPUC (2 members) and the CEC (1 member).
- The Board would execute an Interagency Agreement with DGS to operate the program.
- The Board, in collaboration with stakeholders, would develop programs and eligibility criteria, and these criteria would be incorporated into the contract with DGS.
- Utilities would collect the PGC from ratepayers in an amount and for a duration as determined by the Board.
- Utilities would deposit the funds in a special account with full accounting of amounts by customer class provided to DGS.
- DGS would then administer the distribution of funds in accordance with the criteria developed by the Board.

This set of programs could encompass standard offer programs including rebates, market transformation programs, RD&D grants, and other programs.

DGS is a 3600 person department with an annual budget well over $500 million comprising 21 offices that perform a variety of business functions. There are many boards and commissions throughout government that contract with DGS to manage various aspects of their operation, allowing them to remain small and focused on their policy objectives.

By employing already existing resources in the Department of General Services, and designing programs that efficiently stimulate the marketplace, such as the Voucher System described in the full proposal, DGS believes that these programs can be administered for amounts on the order of 1 percent of the funds being managed. Other more complex, staff-intensive programs will clearly require more than this, but could also be very efficiently managed. There are a number of activities to be performed by DGS to ensure efficient operation of the program:

- Program accounting, reporting, and fund management through the Office of Fiscal Services.
- Contractor selection and contract management for inspection contractors, as well as other program consultants through the Office of Energy Assessments.
- Ongoing maintenance of program staffing.
- Information materials, application and voucher printing, inventory, etc.
- Statewide service for in-person information, application pickup and submittal, and coordination of customer contacts through the Office of Buildings and Grounds in all state office buildings.
- Dispute resolution through the Office of Administrative Hearings (mediation and arbitration services).

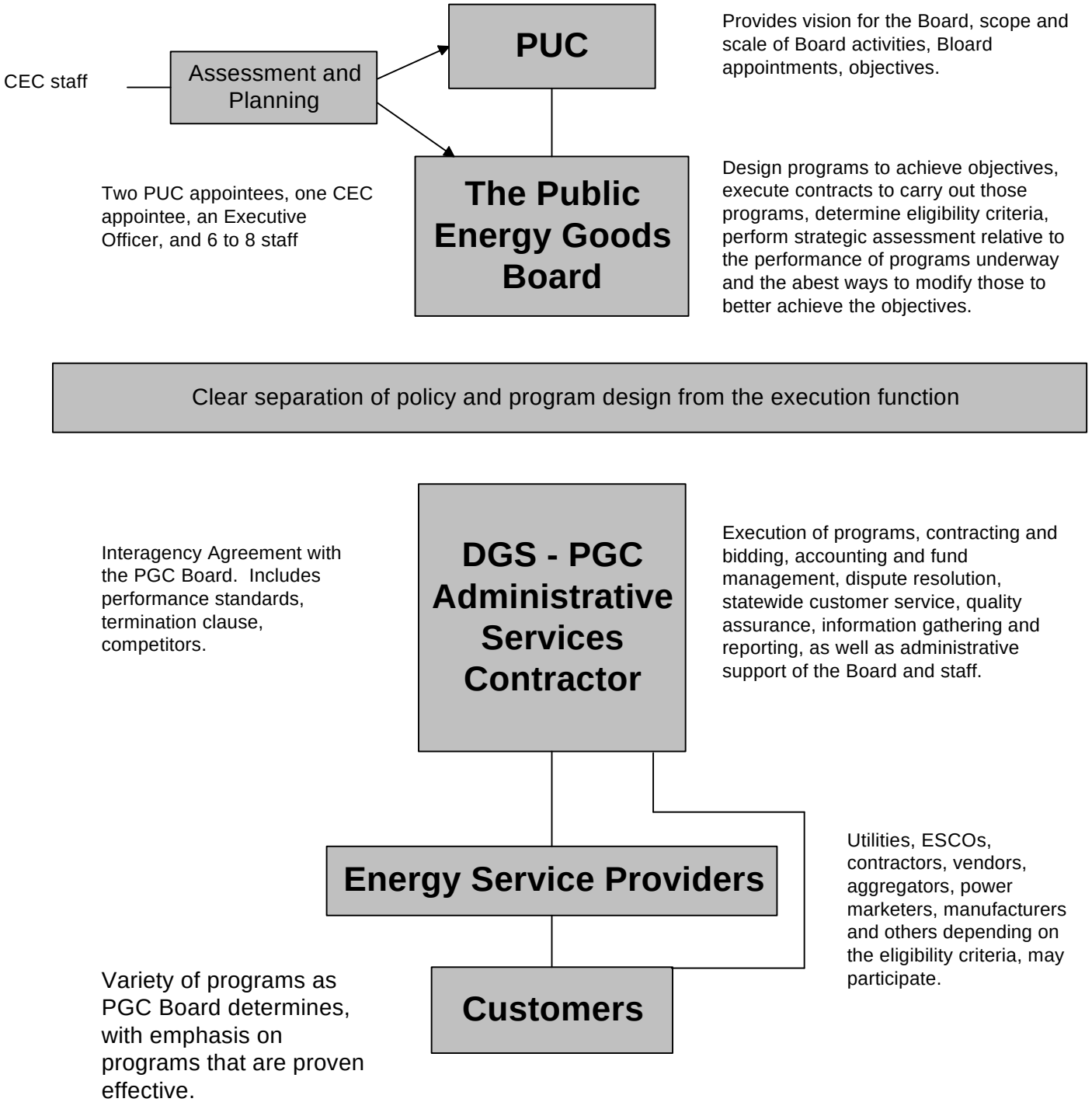
- Regular attendance at Board meetings to provide feedback on the relative success of the various programs undertaken at Board direction, as well as general communication.
- Data collection and reporting for input to the Board's strategic assessment activities.

Competition at various levels of the operation will promote program efficiency overall. Competition at the service provider level as well as at the program administrator level (DGS' contract) should serve to keep down costs and increase efficiency. We expect to include a termination clause and performance standards in the contract.

Other features of this proposal include:

- CPUC would be able to keep control of the process through its contractor, DGS. Modifications after the onset of the program could be easily accomplished via contract amendment.
- CPUC would be relieved of the administrative burden, even that of contracting out, since an interagency agreement is simple to execute and requires no bidding.
- DGS has many similar fund management and construction inspection tasks which it performs currently, giving this proposal a high probability of success.
- Supporting staff and providing continuity would not be difficult, since DGS already maintains staff involved in the various areas described.
- If the Board decides to terminate any of the programs, use of an existing organization such as DGS who is already in this business, and will be after this process is terminated, allows it to start up quickly, and to operate at peak efficiency right to the end.
- This system will provide a material boost to the Energy Service Company (ESCO) industry by placing them on an equal footing with the utilities.
- Dispute resolution can be handled through existing effective mechanisms.
- Use of existing organizations eliminates risk and time lag involved with seeking approval for a new government entity.
- Service will be available through State buildings in all major, and many minor cities throughout the state, as well as over the Internet on the DGS Home Page.
- Opportunities for fraud are minimized.
- Due to low cost of program, and reduction of utility and CPUC costs of regulation, kW and kWh reductions per dollar of PGC will increase.
- DGS is not-for-profit, requires no shareholder incentives, ERAM mechanism, or other cost adders.

Public Goods Charge
Independent Administrator
Organization
Department of General Services
Proposal



Chapter 5

RECOMMENDATIONS TO GUIDE THE TRANSITION TO A NEW PGC ADMINISTRATOR

INTRODUCTION

Many steps need to be taken in the next 18 months to ensure that the new PGC administration can continue to deliver energy efficiency services to customers when restructuring begins on January 1, 1998. This chapter focuses on two types of actions; those that should be taken by the CPUC to ensure a smooth transition toward the pursuit of its market transformation objectives which are independent of the administrative form selected and those that are contingent upon the CPUC's choice of administrative options proposed in the last chapter. In turn, these choices may be contingent on other policy decisions that are currently being addressed in other working groups or hearing processes in restructuring. These key decisions and their linkages to the PGC administration are described in the second section of this chapter.

Two types of transition issues that should be addressed as restructuring unfolds. The first type includes those issues that the CPUC has authority to order or implement under its current area of control. The second type of action requires legislative approval or adoption before they can be implemented. This chapter only deals with the first set of issues, those which the CPUC has the current authority to act upon. Any issues which belong in the second set are covered in the specific administrative proposals in Chapter 4 or discussion of jurisdictional issues in Chapter 3.

STEPS THE CPUC SHOULD CONSIDER INDEPENDENT OF ITS CHOICE OF ADMINISTRATIVE OPTIONS

Three generic issues can be addressed in the next eighteen months: (1) development of a proposed treatment of utility liabilities and assets created by the past decade of public funding for energy efficiency programs; (2) development of a process to encourage pilot testing of new market transformation ideas and measurement approaches; and (3) provision of near term guidance with respect to the design of current utility energy efficiency programs. Each issue is addressed below.

Treatment of Assets, Liabilities, and Ongoing Commitments to Customer Participants

An important issues for the near term is the proposed treatment of potential utility liabilities and assets related to energy efficiency activities which may be or have been incurred or acquired during the transition. Potential liabilities incurred by utilities for current purchases of energy savings include multi-year contracts or other obligations for payments to contractors or customers who provide these savings, beyond the term of the "transition." Potential assets include expectations or contractual agreements for future revenue from shared savings programs currently operated by utilities.

The CPUC should consider issuing an interim decision that provides some guidance as to how these liabilities and assets will be treated in future restructuring decisions. For example, utility program managers would certainly benefit from the provision of some information about the costs and benefits of continuing to make financial commitments to customers or suppliers. Absent a commitment by the CPUC to fully or partially fund current commitments in future years, most parties expect that the level

of program activity may slow considerably in calendar year 1997 if utilities must make commitments without any certainty of cost recovery.

The CPUC must also consider providing some certainty that UDC earnings attributed to past and current energy efficiency programs will also be available to them in future years. As part of this decision, the CPUC should consider if and how it wants to provide the funding necessary to continue to measure and evaluate the effects of previous utility programs as required by the ex-post measurement protocols.

Such guidance is needed as soon as possible in order to ensure that obligations entered into by utilities in 1997 will not be stranded by future CPUC decisions. Any uncertainty regarding these issues can be expected to have a deleterious effect on utility plans for 1997 programs and be detrimental to a smooth transition.

Authorize or Encourage Pilot "Market Transformation" Projects

The CPUC should also consider encouraging parties to begin laying the foundation for the pursuit of market transformation objectives in 1998 by pilot testing ideas, programs and measurement concepts in 1997. These activities should be designed to encourage a shift from resource-driven energy efficiency to energy efficiency driven by market transformation objectives. This includes authorizing pilot programs with market transformation objectives and attempts to verify the market effects of these programs. In addition, to the extent that parties' proposals necessitate the creation of a new set of compensation or incentive mechanisms, these mechanisms must be developed and the treatment of the funds assessed.

Schedule Workshops or A Proceeding in 1997 to Develop Guidelines for New Administrator(s)

In order to deliver PGC-funded activities beginning on January 1, 1998, the administrator will need to be provided with whatever guidelines and other direction found appropriate by the CPUC. Therefore, following selection of a specific administrative option, the CPUC should conduct a proceeding in 1997 to develop any necessary guidelines or operational rules to guide the administration of PGC funds for energy efficiency. At this point, it may also be appropriate to consider revisions to the CPUC current DSM policy rules.

Within the course of this proceeding the CPUC should address the following additional issues:

- Adoption of PGC collection and fund distribution mechanisms and accounting details
- Development of administration guidelines and oversight protocols/functions
- Development of oversight procedures for measurement, evaluation, and customer assurance
- Assurance that the necessary legal/regulatory hurdles to implementation are reviewed and addressed
- Coordination of the recommendations of this report with the other Working Group reports

Several of the administrative proposals described briefly in Chapter 4 and in more detail in the Appendices offer some useful insights and a more detailed timetable for dealing with these and other issues.

Some parties also believe that the CPUC should address the following longer term issues.

- If there are to be significant legislative changes in the administrative system, the CPUC should consider establishing an interim organization under its own authority which could begin the transition process. This strategy should allow for the phasing out of existing programs as program designs with market transformation objectives are developed.

- The CPUC should order a full inventory and audit of existing utility DSM programs prior to implementing new administration of PGC funded programs. This is necessary to ascertain the value or disposition of program assets and liabilities.

RELATIONSHIP OF OTHER RESTRUCTURING DECISIONS TO ENERGY EFFICIENCY ACTIVITIES

Parties recognize that there are a number of other decisions that will be made as part of the restructuring process that will have important effects on the market environment, effectiveness, and capabilities of the new administrator. At a minimum the CPUC's decisions made in the four policy areas listed below will have a significant effect on the goals of the administration and design of energy efficiency activities or programs funded by the PGC.

Decisions Relating to the Structure and Type of Administrative Organizations Used to Implement the Other Public Policy Programs (RD&D, Low Income, Others)

RD&D -- The restructuring decision provides for a complementary set of "public goods" research and development activities to be pursued using funds raised by the PGC. This may require the development of a separate administrator or a separate department within the same administrative organization to implement. In either case, it is desirable to coordinate energy efficiency and RD&D activities. There is a need for parties to address any functional, funding, or governance overlaps that may exist between the recommendations provided in the two working group reports.

Low Income -- The structure or organization selected to deliver services to the low income population segment should at a minimum not work at cross purposes with the new administrative structure for energy efficiency. In fact, there may be some public benefit in asking these management organizations to periodically meet and exchange information on the results of their programmatic efforts.

Decisions Related to the Functional Unbundling of Integrated Utility Companies

The CPUC is currently overseeing the separation of assets of integrated utilities into distribution, transmission and generation subsidiaries or companies. The decisions made here and the rules adopted to prevent cross dealing between these new entities will have an effect on the business missions of distribution companies including their energy efficiency programs.

Decisions Related to Rate Design, Performance Based Ratemaking and Revenue Recovery

Utilities have been asked to propose performance based ratemaking (PBR) mechanisms for their transmission and distribution companies. Utilities or other parties may also propose some form of decoupling mechanisms to separate UDC earnings from sales volumes. CPUC decisions on how UDCs are allowed to earn profits within this new mechanism will definitely have an effect on the

administration of all energy efficiency programs, whether or not they are supported by PGC funds. To facilitate these decisions, the CPUC has encouraged the creation of working groups that are discussed below.

Rate Setting Working Groups -- Subcommittees are addressing how the costs from different electricity functions will be unbundled and displayed on bills, the potential need to shift towards higher fixed costs and lower marginal energy costs on customer bills (particularly to recover distribution costs), how stranded generation and distribution costs will be allocated between customer classes, particularly as some customers opt for direct access contracts, and the overall magnitude and timing of the collection of the CTC. These decisions may affect the cost effectiveness and design of PGC programs and the amount of PGC funding available. Subcommittees of this group are also discussing both the degree and amount of unbundling of utility distribution functions that will be necessary before January 1. 1998. These decisions may have a direct effect on the design and content of energy efficiency programs.

The Development of Direct Access Protocols/Rules/Schedules

The work of at least four working subgroups in this area will affect PGC program design and administration:

Direct Access Working Sub-Groups -- The Market rules subcommittee is addressing how to provide comparable access to customer information assets for both suppliers and energy service firms. This will affect both the targeting strategies of programs and the procedures used to procure energy efficiency services. The Customer Protection subcommittee is considering guidelines to ensure "minimum levels" or quality service for all customers. Some of these guidelines may effect the design of PGC programs. The group is also considering proposals to enhance the benefits received by customers through better billing formats and rules to facilitate the aggregation of residential and small customers to achieve cost savings and energy efficiency benefits. The Metering subcommittee is addressing the need for uniform rules or customer requirements for time-of-use meters, which may affect the cost effectiveness of some energy efficiency investments. Finally, the Implementation subcommittee is addressing the qualifying conditions for direct access which may affect the amount of funding available for the PGC administrator. Most of these decisions will affect the strategies used to target energy efficiency services to customer groups.

The secret of all victory lies in the organization of the non obvious.
To accomplish great things
we must not only act, but also dream,
not only plan, but also believe.
Anatole France

THE END